

Update

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Consultation on FinTech regulation

On 1 February 2017, the Swiss Federal Council issued for consultation proposed amendments to the Banking Act ("BA") and the Banking Ordinance ("BO") aimed at facilitating the emergence of innovative business models based on financial technology ("FinTech"). The proposed risk-based and technology-neutral amendments are designed to lower market entry barriers and include a new type of license for FinTech and other companies accepting public deposits.

Background

Acceptance of more than 20 or public solicitation of deposits, regardless of the amounts involved, currently falls within the definition of banking activity and requires a banking license granted by the Swiss Financial Market Supervisory Authority ("FINMA"). This in turn triggers onerous authorization granting requirements (e.g., minimum equity, liquidity, controls). Obtaining and maintaining such license constitutes a significant barrier to market entry for FinTech and other innovative companies.

General approach

The proposed draft amendments to the BA and BO lower the barrier to market entry for such companies as they often have a reduced business scope as compared to traditional banking and are thus assumed to have a lower risk profile. In line with general Swiss financial market regulation, the proposed amendments are principle-based and technology-neutral. Anticipating that new business models of both FinTech companies and traditional banks will continue to evolve, the new regulation is intended to apply irrespective of the

specific business model and aims at creating legal certainty for all providers of financial services.

Proposed key amendments and rationale

The proposed Swiss FinTech regulation model, by contrast to the approach adopted by other jurisdictions, is based on three "pillars": (1) banking license "light" to cater for the specific risk profile of FinTech business models, (2) creation of an innovation area (i.e., "sandbox"), and (3) "light touch" targeted regulatory adjustments.

Key aspects of the proposed amendments include:

- › **FinTech license:** A new license type is proposed under the draft BA amendments for companies accepting public deposits while not using such deposits to fund the traditional lending business. The aggregate amount of public deposits must not exceed CHF 100 million (a higher threshold may be individually authorized) and may neither be invested nor be interest-bearing. Under such license, companies would be subject

to a more lenient capital adequacy framework. This new license type eases the regulatory burden in cases where FinTech or other companies (e.g., online banking, mobile payment processing, crowdfunding) take deposits while, from a risk perspective, it would seem disproportionate to impose a full traditional banking license given their specific business model.

- › **Innovation area or "Sandbox":** The proposed Sandbox is a concept creating an innovation environment wherein providers of financial services are not subject to licensing as a result of public deposit taking. Under the draft BO amendment, a business would be allowed to accept deposits without a banking license up to an aggregate deposit amount of CHF 1 million and irrespective of the number of public deposits, again provided that – if the business is active primarily in the financial sector – the deposits are not invested and no interest is being paid. The Sandbox allows FinTech and other companies to test and develop business models without blocking the capital and incurring the cost that a full banking license entails. This is of particular relevance for (a) crowdfunding platforms as no time limit applies regarding the CHF 1 million threshold (when compared to settlement accounts; see below), allowing an annual funding volume in excess of the threshold, and (b) SMEs seeking to raise funds through crowdlending.
- › **Duties to inform:** The new type of license and the Sandbox would be subject to certain additional requirements, including a disclosure to the depositor that the provider of financial services does not hold a banking license and that deposits are not covered by the Swiss depositor protection system.
- › **Extended holding period for settlement accounts:** Under the proposed revised BO, third-party monies accepted on accounts for the sole purpose of settling client transactions do not qualify as deposits. As per current FINMA practice, the maximum holding period is 7 days. The draft BO extends this time period to 60 days, allowing

crowdfunding platforms to hold monies during such (collection) time period without requiring a banking license (again provided that no interest is paid and funds are not invested).

- › **No money-laundering exemption:** The proposed amendments do not address anti-money laundering regulations. FinTech and other companies acting as financial intermediaries will generally continue to be subject to anti-money laundering obligations, including compliance with KYC (know-your-customer) rules. However, compliance with Swiss anti-money laundering regulations is easy to achieve and, hence, should not represent a significant entry barrier.

Key implications and next steps

The suggested Swiss FinTech regime addresses the most critical barriers to innovative business models (i.e., regulatory threshold for taking client money and holding more than 20 deposits) and would allow for fair and equal treatment of all market players and provide a better risk-based framework to encourage innovation. In combination with other regulatory relief (notably the FINMA Circular 2016/7 on Video and Online Identification – Due diligence requirements for client onboarding via digital channels), the proposed amendments create new business opportunities for both FinTech companies and other more traditional financial services providers irrespective of the technology used (including by way of collaboration, outsourcing and otherwise).

FinTech and other companies engaged in or servicing the financial sector will need to assess the legal implications (including with respect to technical and organizational measures) as well as business opportunities and risks in order to decide whether their business models are suitable for the Sandbox or whether a FINMA license is required (whether a new FinTech license or a banking license). This applies to many upcoming business models, such as those involving mobile payment, blockchain and related applications, cryptocurrencies, automated investment advice, crowdfunding or peer-to-peer lending.

With respect to the actual requirements applying to the new FinTech license, it is planned that all the other requirements of the BA would apply by analogy. The intended more lenient capital adequacy framework (minimum capital, equity, liquidity, organization) is yet to be set out in implementation provisions.

The consultation ends on 8 May 2017. The draft BA will need to be approved by Parliament.

Interestingly, in its current deliberations of the Financial Institutions Act ("FinIA") the parliament is already discussing the FinTech license and respective amendments to the BA. Thus, the new FinTech regulation may be enacted as early as next year 2018.

Please do not hesitate to contact us in case of any queries. Thank you.

Legal Note: The information contained in this UPDATE Newsflash is of general nature and does not constitute legal advice. In case of particular queries, please contact us for specific advice.

Your contacts

Geneva / Lausanne

Shelby R. du Pasquier
shelby.dupasquier@lenzstaehelin.com
Tel: +41 58 450 70 00

Fedor Poskriakov
fedor.poskriakov@lenzstaehelin.com
Tel: +41 58 450 70 00

Zurich

Lukas Morscher
lukas.morscher@lenzstaehelin.com
Tel: +41 58 450 80 00

Marcel Tranchet
marcel.tranchet@lenzstaehelin.com
Tel: +41 58 450 80 00

Stefan Bürge
stefan.buerge@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
Bleicherweg 58
CH-8027 Zürich
Tel: +41 58 450 80 00
Fax: +41 58 450 80 01

Lausanne

Lenz & Staehelin
Avenue du Tribunal-Fédéral 34
CH-1005 Lausanne
Tel: +41 58 450 70 00
Fax: +41 58 450 70 01

www.lenzstaehelin.com