

Briefing February 2017

FinTech – Federal Council Opens Consultation

On 1 February 2017, the Federal Council launched a public consultation on proposed amendments to the Banking Act (BA) and the Banking Ordinance (BO), which seek to ease the Swiss regulatory framework for providers of innovative financial technologies (FinTech), e.g. crowd-funding and crowd-lending, electronic payment services, robo-advice and crypto-currencies. This legislative project aims to implement the proposals of the Federal Council announced on 2 November 2016 (see Bär & Karrer Briefing November 2016), which should strengthen the competitiveness of the Swiss financial centre. The consultation will last until 8 May 2017.

The proposed amendments to the Banking Act (Draft BA) and the Banking Ordinance (Draft BO; together the Draft Rules) build on the three pillar approach to support FinTech that was presented by the Federal Council in November 2016 by creating two exemptions from the requirement to obtain a banking licence in connection with certain deposit-taking activities and introducing a new type of licence, which would be subject to less stringent requirements, for financial innovators and other interested parties (banking licence 'light'). As expected, the exemptions and reliefs do not extend to anti-money laundering regulations, which will continue to apply to FinTech firms if they act as financial intermediaries.

If adopted, the proposed exemptions and the new licensing regime are expected to lower market entry barriers for FinTech firms, reducing their operational costs and increasing competition in the field. Overall, the new Draft Rules are likely to enter into force at the earliest in 2018, assuming the proposal is received positively by all stakeholders.

Proposed New Rules

Extension of the Maximum Holding Period of Monies on Settlement Accounts

Under current Swiss banking regulations, third-party monies accepted on interest-free accounts for the purpose of settlement of client transactions do not qualify as deposits from the public (article 5 para. 3

lit. c BO). This exemption allows a financial intermediary to hold client monies for settlement purposes without needing a banking licence.

Currently, the Swiss Financial Market Supervisory Authority (FINMA) considers that monies may be held on a settlement account for seven days at most without qualifying as deposits from the public as

defined under banking regulations. The Draft Banking Ordinance proposes to codify this practice and, at the same time, extend the maximum holding period to 60 days. However, to qualify, settlement accounts will need to be non-interest bearing accounts (article 5 para. 3 lit. c no. 1 Draft BO). Moreover, the extension will not apply to settlement accounts of securities dealers (article 5 para. 3 lit. c no. 2 Draft BO), who will continue to be subject to the current regime.

Firms profiting from this exemption will not be supervised by FINMA and will, therefore, not need to comply with prudential requirements and bear the financial burden associated with prudential supervision.

This exemption will benefit firms whose business model requires them to hold on to client monies on settlement accounts for an extended period of time. In particular, crowd-funding platforms will be able to collect funds from the crowd for periods of up to 60 days before forwarding them to the funded project, without requiring a banking licence, as long as they do not pay interest on the monies they receive. Furthermore, payment service providers will also be able to benefit from this exemption, as long as they do not hold funds for more than 60 days.

Innovation Sandbox

The Draft Rules also propose to create an innovation 'sandbox' for FinTech operators and other interested businesses. Such firms will not require a banking licence as long as they do not accept public deposits in excess of CHF 1 million (article 6 para. 2 lit. a Draft BO). This threshold will be measured on the basis of the aggregate deposits held at any given point in time, as opposed to, e.g., a maximum turnover. This means that FinTech platforms can allow significantly more than CHF 1 million per year to pass through their accounts without needing a banking licence, as long as, at any given time, they do not hold more than CHF 1 million in deposits. However, firms that are mainly active in the financial sector will only be allowed to benefit from this exemption if no interest is paid on the deposits and the funds are not invested (article 6 para. 2 lit. b Draft BO). According to the explanatory report on the amendments to the Banking Act and the Banking Ordinance, the term 'investing' has to be interpreted very broadly in this context. It

probably means that the funds received should remain credited to accounts of the firm at all times and cannot be used, e.g. for investment purposes or to fund the working capital needs of the firm.

Finally, a firm making use of this sandbox exemption will be required to inform its customers that it is not supervised by FINMA and that deposits are not covered under the Swiss depositor protection system (article 6 para. 2 lit. c Draft BO).

The innovation sandbox will allow start-ups to develop their projects and to test their business model without incurring the full burden of requiring a banking licence or complying with prudential requirements.

New Licence for FinTech Innovators

Finally, the Draft Rules propose to create a new type of licence, dubbed the banking licence 'light', for FinTech firms and other entities that accept, on a professional basis, a maximum of CHF 100 million in public deposits provided they do not engage in the traditional banking business of maturity transformation (*Fristentransformation*). A higher threshold can be allowed, on a case by case basis, if customers are protected through additional safeguards (article 1b para. 4 Draft BA). The banking licence 'light' will also be conditioned on firms (a) not paying interest to depositors and (b) not investing the deposits (article 1b para. 1 Draft BA).

Holders of the proposed new licence will profit from less burdensome requirements with respect to financial reporting and audits as well as, subject to implementing provisions that are yet to be developed, less invasive organizational, equity, capital adequacy and liquidity requirements. For example, the explanatory report suggests that it will apply a simplified capital adequacy framework requiring firms to hold 5% of the assets on deposit but not less than CHF 300,000 in capital.

Furthermore, deposits held with such firms will not be covered by the Swiss depositor protection system. The holders of a banking licence 'light' will have to inform their customers of this fact (article 1b para. 3 lit. d Draft BA).

In any event, the costs for complying with the requirements of a banking licence 'light' should be substantially lower than those associated with a 'fully fledged' banking licence. At the same time, firms holding such a licence will benefit from the 'quality label' associated with supervision by FINMA, which may make them more palatable to certain clients and investors.

This regime may be of interest, in particular, for e-money issuers and crowd-funding platforms intending to hold client funds for a period exceeding the 60-days limit available for settlement accounts as described above. However, firms using other business models will also be able to profit from this new regime.

Application of Anti-Money Laundering Regulations

The exemptions and reliefs proposed by the Federal Council do not extend to anti-money laundering regulations. FinTech firms acting as financial intermediaries will, therefore, continue, as a matter of principle, to be subject to the duty to join a self-regulatory organization or be directly supervised by FINMA for anti-money laundering purposes and comply with regulatory requirements regarding know-your-customer and anti-money laundering. Furthermore, holders of the banking licence 'light' will be deemed per se financial intermediaries by virtue of their regulatory status (article 2 para. 2 lit. a Draft Anti-Money-Laundering Act).

Impacts on Banks

These exemptions and the creation of a banking licence 'light' will allow new competitors to enter into market segments currently reserved to banks at considerably lower costs. At the same time, banks will continue to be able to enter into these new market

segments directly and take advantage of these exemptions through dedicated affiliates. Moreover, they may also seek to profit from developments in this area, without directly entering into this segment, by entering into joint ventures or outsourcing projects with FinTech firms.

Next Steps

The consultation period for the proposed amendments to the Banking Act and the Banking Ordinance will last until 8 May 2017. In addition, the proposed introduction of a banking licence 'light' will require further amendments to the implementing regulations such as the Banking Ordinance, the Liquidity Ordinance, and the Capital Adequacy Ordinance. In particular, less stringent requirements regarding organization, minimum capital, equity and liquidity will probably apply to these licensees. These further amendments are expected to be subject to a further separate consultation procedure.

To accelerate the legislative procedure, the Economic Affairs and Taxation Committee of the Council of States, one of the chambers of the Swiss Parliament (*Kommission für Wirtschaft und Abgaben des Ständerates, WAK-S*), already proposed in October 2016, in the context of the legislative project for a Financial Services Act (FinSA) and a Financial Institutions Act (FinIA), to amend the Banking Act, creating the basis for a banking licence 'light'. This proposal was accepted by the Council of States on 16 December 2016. The legislative project is now pending with the National Council, whose Economic Affairs and Taxation Committee decided to enter into debates on the FinSA and FinIA on 16 January 2017 and will start its detailed deliberations on the bill on 20 / 21 February 2017. In any event, it is uncertain when these changes will be implemented, although realistically we would not expect them to enter into force before 2018.

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