

MARCH 2019

Newsletter

Authors:

Dr. Olivier Favre, LL.M.

Fabio Elsener, LL.M.



BANKING & FINANCE

Bank License "light" and Swiss FinTech Regulation

The regulatory environment in Switzerland for companies of the financial technology (**FinTech**) sector continues to evolve. A new bank license "light" for a deposit taking activity up to a threshold of CHF 100 million is available from 1 January 2019. Also, the Swiss Federal Council published a report outlining further changes to Swiss regulation in connection with blockchain technology and digital assets.

1 INTRODUCTION

A first package of reforms to foster the regulatory environment in Switzerland for FinTech businesses included the introduction of an **innovation sandbox**, allowing firms to take deposits of up to CHF 1 million without being subject to a bank license requirement (see our newsletter of April 2017). As of 1 January 2019, a new type of bank license (the **FinTech Bank License**) is available. The Swiss Banking Act (**BA**) was amended to that effect.

The FinTech Bank License offers a **new regulatory status for banking businesses** that otherwise would need to obtain a regular bank license or a securities dealer license. Moreover, the legislator expanded the scope of the innovation sandbox available since 1 August 2017.

Looking further ahead, the Federal Council notes that certain points should be improved in the Swiss regulation of the FinTech sector and the rules applicable to blockchain-based digital assets (**Crypto Assets**). In its report of 7 December 2018 on the legal framework for distributed ledger technology and blockchain in Switzerland (the **DLT Report**), the Federal Council

provided an analysis regarding the classification of Crypto Assets under Swiss law and financial markets regulation as well as an **outlook on the changes to Swiss law** we may expect in the near future.

2 ACTIVITIES WITHOUT A BANK LICENSE

2.1 NO RELEVANT DEPOSIT TAKING ACTIVITY

The bank license requirement under Swiss banking regulation is in particular triggered by a **deposit taking activity**. For these purposes, "deposits" are all liabilities except for those carved out according to the BA, the Swiss Banking Ordinance (**BO**) and the circular of the Swiss Financial Market Supervisory Authority (**FINMA**) on deposit taking activities (**FINMA Circular 2008/3**). As regards FinTech businesses, the following carve-outs are particularly relevant:

- > **Debt securities:** At present, the issuance of debt securities does not qualify as a deposit taking activity, where the issuer **publishes a prospectus** that meets the disclosure requirements of the Swiss Code of Obligations (**CO**) for bond offerings. In the context of the implementation of the Federal Act on Financial Services (**FinSA**), this reference shall be replaced with a reference to the new FinSA

prospectus regime. This cross-reference is yet to be finalised following the consultation on the Ordinance to the FinSA (**FinSO**) which ended on 6 February 2019. We expect that, as a result, there will be no bank license requirement if either a prospectus is published in line with FinSA requirements or the offering is exempted from the prospectus requirements under the FinSA rules.

- > **Settlement accounts:** The BO also provides that securities and precious metal traders, asset managers and similar businesses holding deposits in settlement accounts do not conduct a deposit taking activity, where such deposits are (i) not interest bearing and (ii) except where the account is held with a licensed securities trader, **used for the settlement of transactions within 60 days**. This exception is, *inter alia*, available for business models involving the on-transfer of funds (such as money transmitting or crowdfunding). However, the exemption is not available to FX traders holding client accounts as well as cryptocurrency traders with a similar activity.

Unless one of the carve-outs or the sandbox exemption applies (see section 2.2), taking deposits from more than 20 depositors or any public advertisement of a deposit taking activity would trigger a requirement to be licensed as a bank.

"As of 1 April 2019, the deposits held in the sandbox may be interest-bearing and the deposited funds may be reinvested."

2.2 SANDBOX EXEMPTION

According to the innovation **sandbox exemption**, the receipt of **deposits** is permitted without a bank license for an amount of **up to CHF 1 million**, provided that (i) **depositors are informed in advance** that the firm is not subject to supervision by FINMA and that they do not benefit from a depositor protection scheme, and (ii) unless the main business of the firm is of industrial or commercial nature, the deposits are not interest-bearing and they are not reinvested. However, the requirement (ii) will be amended with the effect that the **deposits** held in the sandbox **may be interest-bearing** and the deposited funds **may be reinvested** as of 1 April 2019, provided that the business of the firm must not consist in generating a profit resulting from the difference between (a) the interest income from its lending activity and (b) interest paid on deposits received in its deposit-taking activity. This change is aimed at making the sandbox exemption also available to **lending platforms**, where the platform is the contracting counterparty of the clients and the interests paid on deposits match the terms of the loans provided.

Note that FINMA started a consultation for a revision of the FINMA Circular 2008/3 on 15 March 2019 in order to further define what activities are permitted in the regulatory sandbox. According to such interpretation by FINMA, the activities should not include any investments generating income consisting of interests, but they may include investments generating income resulting from market exposures (e.g. investments in equities, bonds, currencies or crypto-assets).

3 THE FINTECH BANK LICENSE

3.1 TARGET "AUDIENCE"

The new license category aims at promoting FinTech innovation. Nevertheless, as a **technology-neutral regulation**, it applies to all business models. Examples of business models that would be suited for a FinTech Bank License could be for instance:

- > **providing payment or trading services** involving the acceptance of deposits from clients for a period exceeding 60 days;
- > **providing wallets** for Crypto Assets, if the wallet provider has a repayment obligation towards the clients and receives the power to dispose of the stored Crypto Assets without involvement of the clients;
- > **providing brokerage services** in relation to cryptocurrencies to the extent the broker holds the clients' assets for a period longer than 60 days.

3.2 NO EXEMPTION FROM OTHER FINANCIAL MARKET LICENSES

Note that a **FinTech Bank License** at present does not exempt the company from complying with **further license requirements for other licensed activities**. As of 1 January 2020, however, the Financial Institutions Act (**FIA**) will provide that regulated banks according to the BA will be permitted to act also as securities dealer, as asset manager of collective investment schemes, as asset manager of portfolios or as trustee (each as defined in the FIA). Since the implementing ordinance to the FIA do not explicitly state that this also applies to a FinTech Bank License, we would welcome further clarification before the FIA enters into effect.

3.3 REQUIREMENTS

The FinTech Bank License is a new license category for companies that accept **deposits from the public up to a maximum of CHF 100 million**, provided that such **deposits are not re-invested** and they are **not interest-bearing**. This threshold is to be calculated at group level, subject to exceptions from FINMA for manifestly independent companies. Furthermore, FINMA may **increase the CHF 100 million threshold** in particular cases if customers are adequately protected. Further, the FinTech Bank License requires that investors be **informed in advance** about the business model, the services provided and the risks associated with the used technologies, that the deposits are not covered by a deposit protection system and that there is no immediate reimbursement in case of bankruptcy.

In order to be eligible for this license, a company has to meet certain **organizational requirements**. In particular it is required to implement an **effective compliance and risk management** as well as measures for avoiding conflicts of interests. Certain exemptions may apply regarding compliance and risk management requirements for companies with a yearly gross return of less than CHF 1,5 million and a business model with low risks.

Moreover, the **accepted deposits** have to be **held separately** from the company's own funds. The deposits have to be held in the currency they were made **as sight deposits or as highly liquid assets**. Deposits in the form of Crypto Assets have to be held in the same type of Crypto Assets (same cryptocurrency or same tokens) as they were accepted from the clients.

3.4 LIGHTER REGULATION COMPARED TO A REGULAR BANK LICENSE

The provisions of the BA apply by analogy to companies with a FinTech Bank License. However, in certain respects, the regulatory requirements are less stringent, e.g. regarding the organization, risk management, compliance, the qualification of the regulatory auditor and the capitalization requirements. The **minimum capital requirement** is set at 3% of the accepted public deposits and must be at least CHF 300,000. Unlike regular banks, there are **no requirements regarding liquidity and own capital**. However, FINMA may require additional capital on a case-by-case basis depending on the business model.

A company with a FinTech Bank License does not have to adhere to the Swiss deposit protection system.

Moreover, the Swiss National Bank confirmed that it may grant holders of the FinTech Bank License **access to the Swiss Interbank Clearing and sight deposit accounts** with the Swiss National Bank. Such access can be of particular importance for businesses in the payment services sector.

4 EXPANSION OF THE SCOPE OF THE CONSUMER CREDIT ACT (CCA) TO CROWDLENDING PLATFORMS

With the adoption of the FinTech Bank License, the **scope of the CCA** has been expanded to consumer loans organized through **crowdfunding platforms** in order to create a level playing field with consumer loans of professional lenders.

"The Federal Council proposes the introduction of a new license category for trading platforms for Crypto Assets."

5 KEY DEVELOPMENTS ADDRESSED IN THE DLT REPORT

5.1 TRANSFER OF CRYPTO ASSETS

Crypto Assets that are a digital representation of rights against an issuer should be **classified as uncertificated securities (Wertrechte)** and, as a result, any transfer of such Crypto Assets without the involvement of the issuer is currently subject to the rules of the assignment of rights, which require a **written declaration of assignment** by the transferor. The Federal Council acknowledges this as an issue for the further development of the market of securities token offerings and endorses industry **proposals** to introduce **new legislation to allow the transfer** of such assets **by way of register entry on a decentralised register** such as a blockchain. This would allow the transfer of such assets through the blockchain without the involvement of a custodian, as it would be necessary if such assets were held as book-entry securities in a centralised way.

5.2 SEGREGATION OF CRYPTO ASSETS IN BANKRUPTCY PROCEEDINGS

The Federal Council proposes to **modify** the current **bankruptcy laws** to allow the **segregation of data of third parties**, including Crypto Assets, **from the bankruptcy estate** in bankruptcy proceedings. To the extent that clients of a wallet provider do not hold Crypto Assets in cold storage with the wallet provider, but the Crypto Assets

are held in an internet-based storage solution with the wallet provider, it would be unclear at present whether such assets could be set-aside in the bankruptcy of the wallet provider. As a result of the introduction of segregation rights, it should become possible to **set-aside such Crypto Assets held by the wallet provider in its insolvency** for the benefit of the clients.

5.3 NEW FINANCIAL MARKET INFRASTRUCTURE LICENSE FOR BLOCKCHAIN BUSINESSES

Departing from the principle of a technology-neutral regulation, the Federal Council proposes the introduction of a **new license category for financial markets infrastructures for Crypto Assets**. Such license category should permit the operation of a multilateral and non-discretionary trading platform for Crypto Assets qualifying as securities as well as providing post-trading activities in relation thereto. Such roles would – under the current financial market regulation – require the involvement of further financial market infrastructures other than trading venues (e.g. a central counterparty, a central securities depository, a securities settlement system).

With the exception that an exchange may also operate a multilateral trading facility, a financial market infrastructure must currently be operated by a **separate legal entity**. The Federal Council suggests to grant exceptions from this rule for the FinTech sector.

Furthermore, the Federal Council proposes to allow the licensing of entities that are solely operating an organized trading facility (**OTF**) without performing further activities, e.g. as bank. In this context, the Federal Council proposes to explore the possibility of **operating an OTF on the basis of the FinTech Bank License**.

5.4 SCOPE OF ANTI-MONEY LAUNDERING LEGISLATION

The Federal Council considers the current anti-money laundering legislation in connection with Crypto Assets as sufficient for the time being. The Federal Council affirms that **most initial coin offerings (ICO) should be subject to anti-money laundering legislation**. In connection with the **storage of Crypto Assets** on wallets, the DLT Report highlights that only wallet operators that have power to dispose over the private keys relating to the Crypto Assets stored in their wallet solution, so-called **custodian wallets** as opposed to **non-custodian wallets**, are subject to anti-money laundering legislation.

6 SUMMARY AND OUTLOOK

The **FinTech Bank License** could offer an interesting path for (FinTech) companies, depending on their business model, to **allow a deposit taking activity** up to the relevant regulatory limit (i.e. up to CHF 100 million). Further, to the extent that it will be possible to operate an OTF with a FinTech Bank License as discussed in the DLT Report, this would create the possibility to use the new license for Crypto Asset trading platforms.

Moreover, the **DLT Report** suggests that the regulatory environment for Crypto Assets will further evolve in the future. Its **proposals** for the legislation on **recognizing the transfer of tokens** qualifying as securities by way of entry of a transaction on a decentralized register and the **segregation of data in bankruptcy** are welcome developments.

Contacts

The content of this Newsletter does not constitute legal or tax advice and may not be relied upon as such. Should you seek advice with regard to your specific circumstances, please contact your Schellenberg Wittmer liaison or any of the following persons:



Dr. Olivier Favre, LL.M.

Partner in Zurich
olivier.favre@swlegal.ch



Tarek Houdrouge, LL.M.

Partner in Geneva
tarek.houdrouge@swlegal.ch



Dr. Philippe Borens, LL.M.

Partner in Zurich
philippe.borens@swlegal.ch



Caroline Clemetson, LL.M.

Partner in Geneva and Zurich
caroline.clemetson@swlegal.ch



SCHELLENBERG WITTMER LTD / Attorneys at Law

ZURICH / Löwenstrasse 19 / P.O. Box 2201 / 8021 Zurich / Switzerland / T+41 44 215 5252

GENEVA / 15bis, rue des Alpes / P.O. Box 2088 / 1211 Geneva 1 / Switzerland / T+41 22 707 8000

SINGAPORE / Schellenberg Wittmer Pte Ltd / 6 Battery Road, #37-02 / Singapore 049909 / www.swlegal.sg

www.swlegal.ch

This Newsletter is available on our website www.swlegal.ch in English, German and French.