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## After the Big Bang: New FINMA Guidance and Guidelines on Financial Market Infrastructures

After the enactment of the Swiss Financial Market Infrastructure Act, FINMA has issued its first Guidance 1/2016 “Financial Market Infrastructure Act: FINMA’s next steps” of July 6, 2016 on the ongoing implementation process. The Guidance gives updates on (1) the assessment of equivalence of Swiss and EU regulations concerning derivatives trading, (2) the extension of deadlines for several obligations of trading venue participants, securities traders, and organized trading facilities, (3) amendments to FINMA Circulars, and (4) further issues. The deadline extensions not only give the market participants time for technical implementation but also help the Swiss regulator ensure equivalence of Swiss regulations with EU regulations, which still are a moving target. In addition, FINMA has recently issued guidelines for Swiss and foreign trading venues, namely the Guidelines on Submitting Applications for Authorization of Swiss Trading Venues of June 16, 2016 as well as the Guidelines on Submitting Applications for Recognition of Foreign Trading Venues of April 5, 2016.

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## Financial Market Infrastructure Regulation: FINMA has issued a new Guidance and Guidelines

It was certainly a big bang for the Swiss financial market, when the Financial Market Infrastructure Act (FMIA) came into force on January 1, 2016. One main purpose of this piece of legislation was the establishment of a regulatory framework which European authorities would deem equivalent to the regulations of the European Union (EU). Simultaneously, implementing regulations such as the Ordinances on Financial Market Infrastructures by the Federal Council (FMIO) and by the Swiss Financial Market Supervisory Authority (FINMA) (FMIO-FINMA) have been issued.

These were just starting shots for an ongoing implementation process. Now, five months later, FINMA has issued its first guidance, the FINMA Guidance 01/2016 "Financial Market Infrastructure Act: FINMA's next steps" of July 6, 2016 (the Guidance). The main prongs of the Guidance are FINMA's equivalence assessment of foreign regulations on derivatives trading, the extension of implementation deadlines for obligations of several market participants, and forthcoming amendments to FINMA circulars. In addition, FINMA has issued Guidelines on Submitting Applications for Authorization of Swiss Trading Venues of June 16, 2016 as well as Guidelines on Submitting Applications for Recognition of Foreign Trading Venues of April 5, 2016.

### At a glance

The FINMA Guidance gives the following updates on the implementation process following the enactment of the Financial Market Infrastructure Act (FMIA):

- 1. Equivalence:** FINMA is assessing the equivalence of European and other foreign rules and regulations regarding derivatives trading on an ongoing basis. FINMA is also liaising with the European Commission with regard to the recognition of the equivalence of respective Swiss rules and regulations by European authorities.
- 2. Extended deadlines:** The deadlines for compliance with certain obligations of trade venue participants, organized trading facilities, and securities traders have been extended to January 1, 2018. Furthermore, FINMA has suspended the deadlines for the exchange of collateral by counterparties of OTC derivatives transactions as well as for the requirement to trade derivatives on a trading venue or OTF.
- 3. Amendments to FINMA circulars:** By spring 2017, two amended FINMA circulars regarding securities journals and disclosures of securities transactions as well as one new FINMA circular on organized trading facilities (OTFs) are to be expected.
- 4. Further issues addressed by the Guidance:** Finally, FINMA draws attention to the obligation to report derivatives transactions, the clearing

requirement for derivatives transactions, the approval of central counterparties (CCP) and the option of voluntary recognition of foreign OTFs by FINMA.

The following sections will summarize and discuss the main issues 1–4 of the Guidance and report on the new FINMA Guidelines for Applications of Swiss and Foreign Trading Venues.

## Issue 1 of the Guidance: Equivalence

### Background

FMIA subjects derivatives trading to specific obligations with regard to (a) the clearing of OTC derivatives transactions through a central counterparty, (b) the reporting of derivatives transactions to a trade repository, and (c) risk mitigation for OTC derivatives transactions.

Provided that the derivatives contract has a material link to foreign supervisory rules, these obligations are regarded as fulfilled if a market participant has met related obligations under *foreign laws and regulations which are deemed equivalent by FINMA* and if a foreign financial infrastructure is being used for the settlement of the trade has been acknowledged as such by FINMA (art. 95 FMIA and art. 81 sec. 3 FMIO).

Foreign laws and regulations are deemed equivalent if the respective obligations and supervision are comparable to corresponding Swiss rules with regard to their substantial effects (art. 81 sec. 1 FMIO, for further criteria see *ibid.*, sec. 2). This “substantial effects”-standard enables FINMA to take a pragmatic approach.

FINMA’s recognition of equivalence of EU derivatives trading regulations should not bring too many surprises and will rather be a self-check of the regulator, given that Swiss financial market infrastructure law and regulations mirror EU regulations and aim at EU equivalence.

### State of the equivalence assessment

In its Guidance, FINMA notes that initially it will concentrate on assessing the equivalence of the corresponding European regulations. With regard to other jurisdictions, FINMA will assess their equivalence with European regulations, given that equivalence with EU regulations has been a main purpose of the enactment of FMIA (para. 2.1 of the Guidance). The Guidance notes that the European Market Infrastructure Regulation No. 648/2012 (EMIR) and FMIA define very similar regulations for the clearing of OTC derivatives transactions through a central counterparty, the reporting of derivatives transactions to a trade repository, and risk mitigation for OTC derivatives transactions (para. 2.2 of the Guidance).

The Guidance mentions that the European Union has not yet passed all its regulations for derivatives trading. Namely the regulations on the exchange of collateral in the case of OTC derivatives transactions are outstanding. However, FINMA states that, to give financial market participants sufficient lead time for technical implementation, it is recognizing EMIR and the correspondent EU regulations as provisionally equivalent (within the meaning of Article 95 letter a FMIA). Furthermore, FINMA has announced that it would regularly update its equivalence assessment “under due consideration of the regulations then definitively passed by the European Union” and report on its decision (para. 2.2 of the Guidance).

### EU equivalence of Swiss rules

The European Commission will equally assess the equivalence of the Swiss regulations on derivatives transactions to EMIR. FINMA assures that it is staying in contact with the European Commission in this respect (para. 2.3 of the Guideline). In November last year, the European Commission has already determined that

Swiss regulations on central counterparties were equivalent for EMIR purposes. More is to come.

## Issue 2 of the Guidance: Extended deadlines

### Deadlines for trading venues, securities dealers and OTFs extended by the Federal Council

The Swiss Federal Council has decided to extend the deadline regarding the following obligations for one more year from January 1, 2017 to January 1, 2018, to give the market participants more time for technical implementation and to keep pace with the extended timeline for the revision of the European Market in Financial Instruments Directive (MiFID II) (see para. 1, 4.2 and 5.1 of the Guidance).

This deadline extension affects the following obligations (cf. art. 129 FMIO and art. 58a of the Stock Exchange and Securities Trading Ordinance [SESTO]):

#### Obligations of trading venues and OTFs:

- provide pre- and post-trade transparency (art. 129 sec. 1 with art. 27, 28 sec. 2–4/art. 42, 43 FMIO)
- implement effective systems, procedures, and arrangements, and maintain compliance procedures to ensure orderly trading (art. 129 sec. 1 with art. 30 sec. 2/art. 40 second sentence FMIO)
- conclude written agreements with all participants holding a special function, in particular market-makers, in the trading venue (art. 129 sec. 1 with art. 30 sec. 3 FMIO/art. 40 second sentence)
- identify and regulate algorithmic and high-frequency trading (art. 129 sec. 1 with art. 31/art. 41 FMIO)

### **Obligations of trading venues participants and securities traders:**

- Record-keeping duty of participants with regard to orders and transactions in derivatives whose underlying instruments are securities admitted to trading on a trading venue (art. 129 sec. 1 with art. 36 sec. 2 FMIO/art. 58a sec. 1 SESTO with art. 30 sec. 2 SESTO; see also art. 1 FMIO-FINMA detailing the record-keeping and documenting requirements)
- Reporting duty of participants regarding the details necessary to identify the beneficial owner and regarding transactions in derivatives whose underlying instruments are securities admitted to trading on a trading venue (art. 129 sec. 1 with art. 37 sec. 1 letter d and sec. 2 FMIO/art. 58a sec. 1 with art. 31 sec. 1 letter d and sec. 2 SESTO; see also art. 2–5 FMIO-FINMA detailing the reporting requirements)
- Exception from the obligation to report foreign transactions in securities admitted to trade in Switzerland and in derivatives referring to such securities *irrespective* of any agreement on information exchange between trading surveillance authorities or regular information exchange between the supervisory authorities in place (art. 129 sec. 2 FMIO with art. 37 sec. 4 FMIO and art. 32 sec. 3 FMIA/art. 58a sec. 2 with art. 31 sec. 4 SESTO and art. 32 sec. 3 FMIA). This means that only after January 1, 2018 (instead of January 1, 2017) this exception presupposes such an agreement on information exchange or regular supervisory information exchange.

Other obligations are not affected by the deadline extension, e.g. the obligations of OTF operators with regard to authorization and recognition proceedings (art. 38 FMIO), to organizational requirements and prevention of conflicts of interest (art. 39 FMIO), and to the setting of trading rules and criteria for the execution of orders (art. 40 sentence 1 FMIO) (see para. 4.2 of the Guidance).

### **Deadline for the exchange of collateral suspended by FINMA**

Counterparties of OTC derivatives transactions which are not small non-financial parties are obliged to exchange appropriate collateral (art. 110 FMIA). Under certain conditions, intragroup transactions are exempt from this requirement (art. 111 FMIA). The collateral requirement only applies to derivatives transactions which are concluded after a certain deadline which originally for certain counterparties was September 1, 2016 (art. 131 sec. 3–4 FMIO). As the European regulatory technical standards regarding the exchange of collateral in OTC derivatives transactions are still outstanding, FINMA is now exercising its statutory authority to suspend this original deadline and to align it with deadlines set by the future EU regulation (based on art. 131 sec. 6 FMIO) (see para. 3 of the Guidance).

As seen in the example of the exemption of intragroup derivatives transactions from the requirement to provide collateral, deadline extensions prove to be a crucial mechanism to ensure regulatory equivalence. Such exemption from the provision of collateral only applies if, among others, there are no factual or legal impediments to immediate transfers of funds within the group (art. 111 letter c FMIA, see also the correspondent rule in art. 11 sec. 8(b) EMIR). It is still not per-

fectly clear what “legal impediments” exactly means. The Message of the Federal Council on FMIA refers to EU regulations to come, but states that it appears obvious that capital requirements as provided for by regulators throughout the world would not qualify as legal impediments (Message of the Federal Council on FMIA, in: Bundesblatt 2014, 7483 et seq., p. 7579). Whether this interpretation will be equivalent to EU standards is uncertain. At least the Draft Regulatory Technical Standards of the European Supervisory Authorities of March 8, 2016 (articles 37 et seq.) do not per se exempt capital requirements from potential legal impediments to intragroup fund transfers.

### **No deadline so far for the requirement to trade derivatives on a trading venue or OTF**

The Swiss legislator has made the entry into force of the requirement to trade derivatives on a trading venue or organized trading facility conditional on international developments (art. 164 sec. 3 FMIA). The entry into force of the respective requirement in the EU has been postponed to January 3, 2018. For lack of urgency, the Guidance leaves this issue aside (para. 1 of the Guidance).

### **Issue 3 of the Guidance: FINMA circulars to be amended**

The FINMA will have to adapt its circulars, which generally summarize its regulatory practice, to FMIA and FMIO in the near future, namely the FINMA Circulars 2008/4 “Securities Journals” and 2008/11 “Disclosure Requirements for Securities Transactions”. In particular, the amendments will address the reference for identifying the beneficial owners involved in the transactions (art. 3 letter k FMIO-FINMA in conjunction with Art. 37

para. 1 let. d FMIO and Art. 31 para. 1 let. d SESTO) as well as the rules governing exceptions. In addition, FINMA is planning to issue a new circular on OTFs, which will define the regulatory provisions relating the operation of an OTF. The amended circulars as well as the new circular are expected to be subject to consultation by the end of 2016 and to be enacted by spring 2017 (para. 4.3 and 5.2 of the Guidance).

#### Further issues addressed by the Guidance

Finally, the Guidance draws attention to:

- the obligation to report derivatives transactions and related (unaltered) deadlines (para. 6 of the Guidance);
- the clearing requirement for derivatives and related (unaltered) deadlines (para. 7 of the Guidance);
- the approval of Swiss trade repositories on derivatives transactions and the recognition of foreign equivalents. No approval has been granted yet; one application for recognition of a foreign trade repository is being processed by FINMA (para. 6.3 of the Guidance);
- the approval of Swiss central counterparties and the recognition of foreign central counterparties (para. 7.4 of the Guidance). No approvals or recognitions have been granted yet. Applications of current CCPs must be submitted by the end of 2016.

On a side note, the Guidance reminds foreign OTFs, which under FMIA are generally not subject to a recognition requirement, that they may apply for voluntary recognition by FINMA (para. 4.1 of the Guidance). However, foreign OTFs providing services to Swiss participants with regard to derivatives trading will de facto be required to obtain FINMA recognition if and as soon as the duty to trade derivatives via a trading venue or OTFs will be brought into force by the Federal Council (FINMA Guidelines on Submitting Applications for Recognition of Foreign Trading Venues of April 5, 2016, para. VI).

#### Authorization and recognition of trading venues: FINMA Guidelines for Swiss and foreign trading venues

Swiss trading venues need FINMA authorization. Foreign trading venues require FINMA recognition. FINMA has recently issued Guidelines on Submitting Applications for Authorization of [Swiss] Trading Venues of June 16, 2016 and Guidelines on Submitting Applications for Recognition of Foreign Trading Venues of April 5, 2016. These Guidelines set out the required information and documents as well as information and reporting duties.

FMIA sets the following implementation deadlines (art. 159 FMIA; cf. para. V of the Guidelines of April 5, 2016 mentioned above), while it may be mentioned that these deadlines are not affected by the FINMA Guidance 01/2016 discussed above:

- Trading venues which have been

granted FINMA authorization or, respectively, recognition before FMIA came into force must submit a new authorisation/recognition application by the end of 2016. They may continue their business activities until FINMA has decided on their application (art. 159 sec. 1 FMIA). For foreign stock exchanges which have been authorized by FINMA not before January 1, 2013, FINMA will carry out a simplified recognition procedure (para. V of the Guidance for Foreign Trading Venues).

- Currently operating trading venues which had not been authorized or, respectively, recognized by FINMA were required to report to FINMA by July 1, 2016. By January 1, 2017, they must satisfy the FMIA requirements and submit an application for authorization or, respectively, recognition. They may continue their business activities until FINMA has decided on their application (art. 159 sec. 2 FMIA).

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