

- the linkage to economic profit has been replaced by economic performance, but this must reflect the full cost of capital and the risk profile of the institution; and
- commission models, while standard in the insurance industry, are covered by the Circular but clarification has been introduced that it is not the intention to make them impractical.

Other changes reflect the aim to leave the addressees with some flexibility in designing their compensation models. And notably, FINMA did not accede to the many requests to place absolute or relative caps on salaries.

7) Outlook

FINMA so far has applied some restraint in jumping to conclusions and adopting new, draconian regulations in response to the financial crisis. While its new capital and leverage ratios for the two big banks in November 2008 drew criticism from those two institutions, the general sentiment was that these requirements are justified and deserve support. In fact, a general international trend seems to move towards the adoption of leverage ratios. Whether the new regulations for compensation schemes announced on 11 November 2009 receives a similar generally supportive reception is open to debate. More importantly, it will generally be interesting to see whether FINMA will continue to pursue a rather balanced approach towards new regulation or whether it will again shift gears and move towards a “high-speed” implementation of new and aggressive rules and regulations. The author hopes, and calls again, that regulatory restraint will continue to prevail, and with the announcement of the new regulations for remuneration schemes it seems that FINMA tends towards such approach.

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International Administrative Assistance in Stock Exchange Matters

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In August 2009, the Swiss Financial Market Supervisory Authority (FINMA) has published a report that describes the international administrative assistance in stock exchange matters provided by Switzerland. The report reflects the active role of FINMA to respond to criticism expressed by foreign lobbyists with respect to certain Swiss rules on administrative assistance and suggests solutions that comply with Swiss procedural law.

By Petra Ginter

1) Introduction

International administrative assistance in securities matters serves as an important cross-border regulatory bridge between increasingly global activities of financial market players and national market supervision. While the global and multi-jurisdictional business of many banks and securities dealers (and their need to invest assets under management in large foreign capital markets) is generally not restricted by jurisdictions, effective market supervision and investigations are – as an act of state – usually restricted to the geographic boundaries of a national supervisor. Accordingly, statutory and regulatory provisions in a specific jurisdiction on mutual assistance are deemed to be an important instrument to facilitate effective (global) market supervision.

The roles of supervisory authorities in international co-ordination matters vary significantly from one country to the other. Some supervisory authorities, such as the US and other significant European countries, *i.e.*, primarily the supervisory authorities of important stock exchanges and liquid capital markets, on the one hand, usually request for international administrative assistance. On the other hand, countries like Switzerland and the UK, *i.e.*, countries in which many financial intermediaries as well as an important international clientele are domiciled, in most cases, are recipients of requests to provide international administrative assistance. Some countries require that financial institutions which act as securities dealers on their capital markets immediately disclose upon request the beneficial owner on whose behalf the trades were made. Accordingly, in case a financial institution is active on these markets, it should be in a position to immediately provide such information in order to avoid the risk of regulatory non-compliance as well as potential regulatory sanctions. As a consequence, it is argued that respective clients should contractually authorize the financial institutions to provide such information directly to the supervisory authority.

Article 38 of the Stock Exchange Act (SESTA) permits international administrative assistance in stock exchange matters, taking into account the interests of both, the foreign financial supervisory authorities and the clients affected by the administrative assistance.

2) Applicable Rules of Article 38 SESTA

Under article 38 SESTA (as amended in 2006), FINMA may provide administrative assistance to foreign supervisory authorities under certain conditions. In its August 2009 report FINMA provides guidance on its application of article 38 SESTA and its interpretation of certain key principles which can be summarized as follows:

- **Request from competent foreign authority:** The request must be lodged by a foreign authority that supervises stock exchanges and trading in securities as regulatory body (such as *e.g.*, the US Securities and Exchange Commission (SEC)) and the request for assistance has to be addressed to FINMA.

- **No fishing expedition/principle of proportionality:** The request must substantiate and specify the information sought and explain why such information is relevant for the foreign authority to supervise its stock exchanges and the trading in securities. In the field of insider trading, administrative assistance is provided if the foreign authority sufficiently shows a *first or prima facie suspicion*, which usually is deemed to be sufficient if, for instance, a trading in certain securities subject to higher volatility or volume is followed by an announcement such as a restructuring of the company. Information on third parties that are not related to the matter subject to the request (*unrelated third parties*) must not be transferred. According to precedents of Swiss courts, it is, for instance, sufficient that an account of a client was used for a doubtful transactions without knowledge of such client to disqualify such client as unrelated third party. FINMA's practice does, however, exempt clients with (written) discretionary asset management agreements from disclosure, subject to restrictive and clearly defined conditions (*e.g.*, the asset management agreement had been concluded long before the doubtful trades took place, the doubtful trades were made without knowledge of the client, and no other factor indicates that the client was involved in the trades). This exemption is considered a specialty of the Swiss administrative assistance system on stock exchange matters.
- **Principle of confidentiality:** Administrative assistance is only provided if the foreign supervisory authority is bound by authoritative or professional secrecy. The duty of a foreign supervisory authority to inform the public of its proceedings (so-called *litigation release*) does not frustrate the administrative assistance. Since the revision of article 38 Sesta in 2006, FINMA has, however, not been obliged to verify whether the (third party) authorities to which information is transferred (by the requesting foreign authority) do also comply with the principle of confidentiality. The former so-called *long arm principle (Prinzip der langen Hand)* according to which the Swiss Federal Banking Commission (SFBC) (today FINMA) was obliged to control and approve every additional transfer of information within the requesting (foreign) country (and, therefore, required for every additional transfer a specific request which could again have been subject to a *specific client procedure* (as described below under 3)), has been abandoned.
- **Principle of specialty:** Administrative assistance is only provided if the foreign supervisory authority will use the information exclusively to enforce (foreign) rules and regulations on stock exchanges, securities trading and securities dealers or for transferring such information for the specific purposes sought in the (original) request to other authorities, courts and bodies. On the one hand, since the revision of article 38 Sesta in 2006, the receiving (foreign) authorities have been authorized to transfer information to criminal authorities in order to prosecute offences against the financial market laws (insider trading, market manipulation, activity without respective license, operating fraudulent Ponzi schemes, etc.) without special or addi-

tional approval by FINMA. In other words, the transfer of information to third party authorities does not require a so-called *reciprocal criminal liability* (*doppelte Strafbarkeit*) any longer. On the other hand, the specialty principle prohibits to use the transferred information for tax purposes or to use the transferred information in the context of criminal procedures which are not associated with the financial markets supervisory law, without prior approval by FINMA and the Swiss Federal Office for Justice (*Bundesamt für Justiz*), *i.e.*, in order to use the requested information for such purpose, a dual criminal liability would be required.

Thus, the revision of article 38 SESTA in 2006 has already facilitated the administrative assistance in stock exchange matters with respect to two important points: (1) the foreign authority that has received information by FINMA may transfer such information also to third party authorities (including criminal bodies) for the exclusive purpose of enforcing (foreign) rules and regulations on stock exchanges, securities trading and securities traders; and (2) the foreign authority is permitted to use such information in enforcement procedures, even if the procedure of the authority will be published to a large extent.

3) Some Practical Aspects and Specific Problems

Control of the formal requirements by FINMA: Upon receipt of a request for administrative assistance in stock exchange matters, FINMA controls whether the formal requirements, namely the *specialty and confidentiality principles* as well as the existence of a *first suspicion*, have been met. In case these formal requirements are not fulfilled, FINMA returns the request to the requesting authority for amendment. In case the request lacks a first suspicion, FINMA rejects and informs the requesting authority, respectively. The test of first suspicion needs to be met in relation to the potential and alleged breach of law. The Swiss Federal Administrative Court (*Bundesverwaltungsgericht*) does not set the bar too high for the requesting (foreign) authority to show that the first suspicion has been met, because, usually, the investigating authority has just begun its investigations, and the Federal Administrative Court understands administrative assistance as a tool to support and not frustrate investigations conducted abroad. *E.g.*, in case a potential insider trading activity is investigated, it generally suffices that the transactions have been entered into within a period of time during which non-public information or events occurred that had an influence on the market price of the respective securities. It is, however, not a decisive factor whether the transactions have led to a profit or seem plausible with a view to the non-public information/event in question. In addition, the actual development of the market price and the transaction volume are perceived irrelevant. In case the formal requirements are fulfilled, FINMA forwards the request for administrative assistance (or, upon consultation with the requesting authority, a respective summary without disclosing any confidential information on the foreign investigation) to the relevant securities dealers.

Duty to inform and report to FINMA: Persons and entities that are supervised by FINMA must provide FINMA with all information and documents that it requires to carry out its tasks, including international administrative assistance (article 29 and 42 (2) Financial Market Supervisory Authority Act (FINMASA)). Any person that provides false information to FINMA is subject to criminal sanctions (article 45 FINMASA) and may also be exposed to administrative sanctions. Even entities that are not subject to FINMA supervision, such as independent asset managers or private investors, are obliged to provide information to FINMA which are necessary to provide administrative assistance to the requesting (foreign) authority. This practice corresponds to the purpose of SESTA to supervise not only stock exchanges and securities dealers, but the financial markets in general. At this stage of procedure, FINMA prohibits the addressee of the request to inform potentially affected clients of the administrative assistance.

Institution-related vs. client-related information: FINMA differentiates between information concerning the supervised financial institution as such, its proprietary trading, its organization, bodies and employees (so-called *institution-related information*) and information that relates to a specific client (so-called *client-related information*). Whereas institution-related information can be transferred to the requesting authority without formalities if the legal requirements for the administrative assistance are fulfilled, client-related information is subject to the *specific client procedure*. To provide clients with certain procedural rights in the context of an international administrative assistance procedure is a specialty of Swiss administrative law compared to most other countries. Accordingly, the Federal Act on Administrative Procedures (*Bundesgesetz über das Verwaltungsverfahren (VwVG)*) applies in case the transferred information contains particular *client data*. As a consequence, FINMA is required to inform the respective clients on the administrative assistance procedure as well as on its right to request a formal decision by FINMA (costs are up to CHF 15000) if the client refuses such transfer of information to the (foreign) authority. Such FINMA decision can be challenged before the Federal Administrative Court within ten days upon receipt (as final court of appeal). The client procedure is highly controversial on an international level, in particular, because it requires disclosure of the request for administrative assistance to the affected client and, accordingly, may imply the risk of collusion and loss of evidence. Although precedent suggests that the success of an appeal is very low (since 2002 no appeal has been approved), it is not unusual that affected clients use this legal remedy. Therefore, FINMA is considering to withdraw the *suspensive effect (aufschiebende Wirkung)* of the appeal for clear-cut cases, and to petition the Federal Administrative Court to uphold this decision. If the client agrees with the transfer of information, FINMA forwards the information to the requesting (foreign) authority.

Defense of the affected clients: The investigations that are underlying the administrative assistance request are carried out abroad and concern a foreign market. FINMA neither has the resources and funds nor the legitimation to control whether the person affected by the administrative assistance has actually violated foreign rule or regulations. The role of FINMA is limited to the control of the formal requirements as described above.

4) Some Closing Comments

FINMA considers article 38 Sesta as a balanced and workable compromise between an efficient administrative assistance to foreign supervisory authorities, on the one hand, and the observance of the procedural rights of a client being affected by the administrative assistance, on the other hand. Yet, FINMA mentions in its report that the current wording of article 38 Sesta has caused criticism from some foreign supervisory authorities and lobbyists because of the special features of the Swiss administrative assistance as mentioned above, mainly the duty to inform the affected person prior to the transfer of respective client-information to the requesting (foreign) authority. This criticism has also led FINMA not to sign the Multilateral Memorandum of Understanding enacted by the International Organization of Securities Commissions (IOSCO) at this stage. With respect to the mentioned concerns, FINMA is currently analyzing possible means, available within the boundaries of applicable law, to delay the information of the client in clearly defined cases (exemptions) in order to avoid the risks of collusion or loss of evidence.

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Eliminating Broker Discretionary Voting for Director Elections – Impact on Foreign Private Issuers

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The US Securities and Exchange Commission recently approved an amendment to the New York Stock Exchange Rule 452, eliminating broker discretionary voting for director elections. This amendment, which will come into effect on 1 January 2010, has no impact on foreign private issuers.

By Thomas Werlen / Stefan Sulzer

On 1 July 2009, the US Securities and Exchange Commission approved the New York Stock Exchange's (NYSE) amendment to Rule 452 (Giving proxies by Member Organizations), eliminating the ability of brokers to vote in their discretion with respect to elections of directors.