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Switzerland: Financial Sector Assessment Program—Detailed Assessment of Observance of Financial Sector Standards and Codes

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FINANCIAL SECTOR ASSESSMENT PROGRAM

DETAILED ASSESSMENT OF OBSERVANCE OF FINANCIAL SECTOR STANDARDS AND CODES

SWITZERLAND
MAY 2002

INTERNATIONAL MONETARY FUND
MONETARY AND EXCHANGE AFFAIRS DEPARTMENT

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I. BASEL CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

This chapter provides the findings from the assessment of Basel Core Principles for Effective Banking Supervision (Basel Core Principles or BCP).[1]

Information and methodology used for assessment

The Swiss authorities were requested to complete a self-assessment questionnaire in advance of the mission pertaining to the above-mentioned regulatory standards and principles. The questionnaire and self-assessments, where performed, were made available to the peer group of experts in advance of the mission. During the mission, the responses to the questionnaire and self-assessments of compliance with the standards and principles were clarified and checked through subsequent discussion with the authorities and market participants in critical areas. In the case of the Basel Core Principles, the banking specialists reviewed documents made available in advance of the mission, met with host country supervisors in the United States and the United Kingdom of the largest two Swiss banks (the Credit Suisse Group and UBS), and spent several days interviewing representatives of the Swiss Federal Banking Commission (SFBC), bankers, bankers association representatives, and accountants in order to clarify and/or verify the facts contained in the questionnaire responses.

The responses to the IMF questionnaire by the Swiss authorities, detailed information available on the SFBC's Internet website (http://www.ebk.admin.ch/) plus the websites of KPMG Switzerland, the Swiss Bankers' Association (SBA), the Federal Department of Finance (FDF), and the two large Swiss banks, facilitated the initial drafting of this report. The Basel Core Principles assessors were able to focus their discussions and verify information provided with the *Federal Law on Banks and Savings Banks of November 8, 1934* (Banking Act), as amended through April 22, 1999, the Ordinance of the Swiss Federal Council on Banks and Savings Banks of May 17, 1972 (Banking Ordinance), as amended through October 4, 1999, other ordinances and SFBC Circulars and Guidelines, Codes, Conventions and Agreements issued by the SBA. Implementing Swiss regulations, SFBC administrative notices and statutory instruments, audit and accounting guidelines and the SFBC's Guidelines on *Financial Statement Reporting Requirements,* which provide instructions/guidance for periodic financial and prudential reports, were incorporated into the assessment process. Follow-up questions were discussed with SFBC staff and supplemental information was provided to the banking specialists as necessary.

Institutional and macroprudential setting, market structure overview

Banking is one of the prime industries in the Swiss economy accounting for significant employment opportunities and contributing 11 percent to GDP. Bank activities have

[1] The main authors of this assessment were Peter Hayward (IMF), Kathleen O'Brien (OCC, United States), and Stefan Spamer (Bundesbank, Germany). The assessment is based on information available during the Financial Sector Assessment Program (FSAP) mission in October 2001.

undergone changes in the last decade with reduction in bank savings accounts, increased investment funds, initiation of mortgage backed securities, increased global custody, fiduciary business, derivatives and investment counseling, and asset management business. Swiss banks offer global consultancy services, primarily in private banking that include tax, pension plan and inheritance counseling.

There are 375 banks licensed in Switzerland.[2] The number of banks has been shrinking in the last decade due to increased competition, mergers and acquisitions. The banking sector is dominated by three large Swiss-licensed banks (part of two banking groups) with significant global presence. There are 24 cantonal banks, 103 regional banks, one cooperative bank (with 537 independent members), 17 private banks, 23 subsidiaries of major international financial conglomerates and 204 institutions categorized as "other banks."

The two largest banking groups represent about 60 percent of total Swiss banks' assets and deposits and dominate the Swiss banking system. The spread of their operations into many different financial markets—including both banking and insurance—in many different countries, which resulted from an extended process of national and international mergers and acquisitions, has significantly complicated the establishment and management of their risk profile, both for their managements and supervisory boards, and for the supervisors. Recently, these large and complex financial institutions have been affected by turmoil on international financial markets. These two aspects – their increasing complexity and their sensitivity to international asset market developments – as well as their key role within the Swiss financial system underscore the importance of an intense, hands-on, and risk-based form of monitoring and supervision by the banking supervisor, including with regard to aspects of corporate governance in these large and often culturally diverse organizations.

The authority and responsibility of the SFBC in bank licensing and supervision are explicitly set out in the Banking Act and various ordinances, circulars, and guidelines. All credit institutions are subject to supervision and regulation by the SFBC. The SFBC is not responsible for the supervision of insurance companies, insurance intermediaries, investment advisors or industrial deposit-taking entities. Thus these entities are not included in this BCP assessment. However, recent recommendations issued by an expert working group include legislation to transfer the supervision of insurance intermediaries to the SFBC.

General preconditions for effective banking supervision

The SFBC and Swiss Government have achieved a high degree of implementation of the recommendations of the Basel Committee's reports. Although not a member of the European Union (EU), Switzerland has incorporated many of the EU Directives into its ordinances, guidelines and supervisory practices. To a large extent, the Basel Core Principles parallel the EU Directives and this contributed to Switzerland's compliance with the Basel Core Principles. The SFBC has recently taken steps to enhance its supervisory process by

[2] As of end-2000 (Swiss National Bank).

establishing a separate Large Bank Supervision unit to oversee the two large banking groups. The SFBC has also created a unit responsible for the assessment and validation of bank models. These two new units, focused primarily on the two main banks, have somewhat altered the traditional Swiss "indirect" supervision of these two banks. The changes allow the SFBC to better coordinate its supervisory activities for the two large banks with external auditors, bank management, foreign host supervisors, and the insurance supervisors. This approach shifts limited supervisory resources to the financial sector's greatest risk, that is, the largest banks. The risk-based supervision approach more fully integrates the SFBC's off-site analysis of these banks' prudential returns with the bank examinations performed by SFBC-licensed and approved external auditors. The new approach includes quarterly management meetings with the two institutions, semi-annual trilateral meetings with the U.K. and U.S. supervisors and the SFBC and annual trilateral meetings with the bank, its external auditor and the SFBC. Cooperation between the SFBC and the Swiss insurance supervisor has also been strengthened.

The overall assessment of the peer review team is that Switzerland is generally in compliance with the Basel Core Principles with two exceptions where the SFBC is deemed largely compliant. The two exceptions are in the area of budgetary independence and banking activities not subject to SFBC supervision. Both exceptions are discussed in more detail in the detailed assessment that follows. It is important to note that the assessment tailored the principles to the Swiss market. Switzerland has a relatively unique banking sector, with a high market concentration by the two largest domestic banks, and a relatively low level of complex bank activities conducted in most other banks, which are primarily involved with mortgage banking activities or private banking and asset management

Currently the SFBC—which is a small organization in comparison to the size of the system it oversees—relies heavily on the dualistic system of supervision whereby the on-site examinations are outsourced by the SFBC to approved and licensed external auditors. The supervisory process is enhanced by the self-regulatory activities of the industry via the Swiss Bankers Association (SBA) who, together with the SFBC issues guidance to the industry. The SFBC is aware of the risks of outsourcing on-site work and takes a number of steps to check that the work done meets the standards required. This dualistic approach, however, would benefit from a more formalized quality assurance program for supervising external auditors and an increase in joint on-site inspections. This, as well as preparations for the new Basel Capital Accord, will require the SFBC, among other things, to recruit and retain a sufficient number of additional competent staff. The SFBC is taking steps in this direction.

Frequent communication between the SFBC and the banks and the external auditors is key to the Swiss current supervisory process. The SFBC's licensing and supervisory policies and practices are clearly communicated to the banks and external auditors. As a member of the Basel Committee, the Joint Forum, and several other international standards and principle-setting bodies, the SFBC participates in setting the standards for financial sector supervision and actively strives to implement them.

The SFBC will continue to be challenged by innovative licensing proposals (such as Internet banks) and requests for approval of new business activities and increasingly complex investment products, many of the same issues being faced by supervisors in other financially developed countries. As banks expand or enter new businesses, supervisors need to remain vigilant in their supervision in order to minimize associated risks in the industry. This should include a more formalized system of supervision with more explicit supervisory directives being incorporated into the Banking Act. The SFBC is responding to recent regulatory initiatives put forth by various expert commissions and working groups to enhance the supervisory process. Several recommendations have come out of these projects and are being considered by the government as a good start in closing supervisory gaps among all financial companies.

Swiss legislation, SFBC ordinances and circulars, or SBA guidelines and circulars cover all the Basel Core Principles. Although the Banking Act is broad in some instances, the SFBC's implementation of the Banking Act through regulations and guidance to external auditors in their examination mandate reflects effective supervision and works well with the Swiss-licensed institutions.

Various expert commissions and working groups have been created in the last several years to analyze the Swiss financial system and supervision. In December 1998, Switzerland's Minister of Finance mandated an expert commission "Financial Market Supervision," chaired by Prof. Zufferey, with an analysis of the strengths and weakness of the system for the supervision of the financial services industry in Switzerland. In November 2000, the expert commission issued a report and 42 general recommendations for a reform of the supervisory framework in the financial sector ("Bericht über die Finanzmarktregulierung und –aufsicht in der Schweiz," *Zufferey Report*).

In May 1999, Switzerland's Finance Minister mandated an expert commission to review the existing bank reorganization and liquidation law and the deposit insurance system. In October 2000, the Expert Commission submitted its findings in a report along with a proposal for an amendment to the Banking Act. The trigger that started that reform process was the failure of the Spar and Leihkasse Thun in 1991, a large regional bank. This incident had brought several shortcomings of the existing legal framework for dealing with insolvent banks to the surface.

In February 2000, the SFBC mandated a working group, chaired by Prof. Nobel, with an analysis of the dualistic concept of the supervisory system. The working group published its report and 17 recommendations in December 2000. In March 2001, the working group "Auditing and Supervision of Banks" was established to follow up on those recommendations and put forward proposals to revise the Banking Act, the Banking Ordinance and the SFBC Circulars to implement the expert commission's recommendations.

In November 2001, the Federal Council instituted an Expert Commission with nine members that will be chaired by Prof. Zimmerli. The Expert Commission was mandated to put forward a legislative proposal for the creation of a unified financial supervisory authority. While the

mission team was aware of the work of the various commissions and working groups, it was agreed prior to the start of the mission that the assessment of the Basel Core Principles would be done based on the laws, policies, and procedures in effect as of the start of the mission. This Basel Core Principles assessment arrived at many of the same conclusions as those of the commissions and working groups, and generally supports the various groups' recommendations.

At this time (and pending the revision of the Banking Act) a potential vulnerability exists because nonbank industrial deposit-taking entities and certain nonbank asset management/investment advisors are not under the SFBC's supervision or covered by the Basel Core Principles. There is vulnerability anytime non-regulated institutions compete with regulated institutions in banking-type activities.

Principle-by-principle assessment

The following assessment of the Basel Core Principles (BCP) is based on the Core Principles Methodology of the Basel Committee on Banking Supervision, October 1999. The methodology makes a distinction between "essential" and "additional" criteria. Essential criteria should be present in order for supervision to be considered effective. Additional criteria further strengthen supervision and countries should strive to implement as many of the additional criteria as possible. This assessment takes both the essential and additional criteria into consideration. Principle 15 on anti-money laundering supervisory activities was supplemented with the August 15, 2001 draft methodology paper issued by the IMF to further facilitate assessments of this particular area and a separate report on anti-money laundering efforts was prepared.

The Basel Core Principles are grouped into seven categories: (1) Preconditions for Effective Banking Supervision; (2) Licensing and Structure; (3) Prudential Regulations and Requirements; (4) Methods of Ongoing Banking Supervision; (5) Information Requirements; (6) Formal Powers of Supervisors; and, (7) Cross-Border Banking.

Table 1. Detailed Assessment of Compliance with the Basel Core Principles

Principle 1.	**Objectives, Autonomy, Powers, and Resources** An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks. Each such agency should possess operational independence and adequate resources. A suitable legal framework for banking supervision is also necessary, including provisions relating to the authorization of banking establishments and their ongoing supervision; powers to address compliance with laws, as well as safety and soundness concerns; and legal protection for supervisors. Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Principle 1(1)	An effective system of banking supervision will have clear responsibilities and objectives for each agency involved in the supervision of banks.
Description	The Swiss regulatory policies are formulated on three levels. The first two, as mentioned above, are issued by Parliament (all acts such as the Banking Act) and by the Swiss Federal Council

	(ordinances based on parliamentary acts). The SFBC has substantial influence on the drafting process of regulatory statutes, but agreement by the SFBC is not intended. On more technical policies, the SFBC has powers to issue prudential regulations. The Banking Act is regularly supplemented by amendments, circulars issued by the SFBC, and, as an outcome of the supplementary self regulation system, the Swiss Banking Association issues guidelines with the approval of the SFBC to meet the regulatory needs arising out of the changing industry conditions. The SFBC makes extensive use of this power. The Federal Law on Banks and Savings Banks (Banking Act), based on the Federal Confederation, entered into force on November 8, 1934 (as amended April 22, 1999) and the Banking Ordinance entered into force on May 17, 1972 (as amended October 4, 1999) providing the statutory and legal framework for banking and the agencies involved in banking supervision. In addition, various other ordinances serve as extensions of the Banking Act: – Ordinance of the SFBC on Foreign Banks in Switzerland of October 21, 1996; – Ordinance of the Swiss Federal Department of Finance on the Percentage for the Cash Liquidity of November 26, 1987; – Implementing Ordinance on the Federal Law on Banks and Savings Banks of August 30, 1961, as amended May 17, 1972; and – Ordinance of the Swiss Federal Court on Arrangements with Creditors of Banks and Savings Banks of April 11, 1935, as amended June 5, 1996. The various provisions of these acts cover monitoring the activities of banks regarding conformity with laws, compulsory prudential ratios and regulations and, within its jurisdiction, enabling the SFBC to take measures necessary to ensuring adherence to laws, norms and regulations. The Banking Act and the Banking Ordinance lay down the framework of minimum prudential standards that banks must meet. Under Art. 23, the Swiss Federal Banking Commission (SFBC) is the sole agency carrying out banking supervision in Switzerland for all banks. Art. 23 of the Banking Act enables the SFBC to take steps to achieve the orderly resolution of problem banks including restructuring or closure. There is no legal basis for forcing a problem bank to merge with another institution. But indirectly, the SFBC is searching for such a solution. Presently 21 circulars are issued and published by the SFBC. In certain fields the SFBC officially backs (but does not formally approve) self-regulatory guidelines issued by the banking industry (e.g., codes of conduct in securities dealing). Whenever the SFBC gives this type of official backing it may also exert substantial influence in the issuing process. If the SFBC is not satisfied with the outcome of self-regulation it may prefer to issue an official regulation: *SFBC Circulars* – Circular 72/1 on Public Solicitation of Deposits of September 14, 1972 – Circular 81/1 on Recording of Precious Metals of April 30, 1981, as amended February 1, 1995 – Circular 86/1 on Monies from Blocked Pension Arrangements of May 6, 1986, as amended February 1, 1995 – Circular 90/3 on Cash Liquidity of December 17, 1990 – Circular 92/1 on Approval and Notification Requirements for Stock Exchanges, Banks, in Securities Dealers and Banking Auditors of September 24, 1992, as amended July 1, 1999 – Circular 93/1 on the Interrelationship between Banking Law and Revised Company Law of August 25, 1993, as amended February 1, 1995 – Guidelines of the SFBC on Financial-Statement Reporting Requirements set out by Arts. 23 to 27 of the Ordinance on Banks and Savings Banks of December 14, 1994, as amended October 28, 1999 – Circular 95/1 on the Internal Audit of December 14, 1995 – Circular 96/3 on the Audit Report: Form and Content of October 21, 1996, as amended

	October 28, 1999 – Circular 96/4 on Acceptance on a Professional Basis of Deposits from the Public by Nonbanks in the Meaning of the Federal Law on Banks and Savings Banks of August 22, 1996, as amended August 26, 1999 – Circular 96/5 on the Legal and Personal Separation of the Fund Manager from Custodian Bank, Delegation of Investment Decisions and Partial Duties of November 14, 1996, as amended October 1, 1997 – Circular 96/6 on the Maintenance of the Security Journal by Securities Dealers of October 21, 1996 – Circular 97/1 on Guidelines Governing Capital Adequacy Requirements to Support Market Risks of October 22, 1997, as amended October 1, 1999 – Circular 97/2 on the Applicability of the SFBC Circulars Concerning Banks to Securities Dealers of November 20, 1997 – Circular 98/1 on Guidelines for the Combating and Prevention of Money Laundering of March 26, 1998 – Circular 98/2 on Commentaries Regarding the Definition of Securities Dealer of July 1, 1998 – Circular 98/3 on Recognized Rating Agencies of July 1, 1998, as amended June 1, 2001 – Circular 99/1 on the Measurement, Management and Monitoring of Interest-Rate Risks of March 25, 1999 – Circular 99/2 on Outsourcing of Business Areas of August 26, 1999 – Circular 99/3 on Early Information Following the End of the Business Year October 28, 1999 – Circular 00/1 on Less Restricted Risk-Diversification Requirements for Claims with Residual Maturity of up to One Year from Banks of October 26, 2000 *Self-Regulation* – Guidelines of the SBA on the Handling of Domestic and Foreign Counterfeit Money of December 11, 1990 – Convention XIX on Notes of Foreign Debtors of May 1, 1987, as amended January 31, 1996 – Agreement on the Protection of Depositors in the Case of Compulsory Liquidation of a Bank, July 1, 1993 – Recommendations of the SBA on Trusteeships of June 22, 1993 – Guidelines of the SBA on the Settlement and the Assessment of Mortgage Loans (Direct and Indirect) of December 23, 1993 – Guidelines of the SBA for the Risk Management in Trading and in the Use of Financial Derivatives of January 31, 1996 – Practices in Foreign Exchange Trading of December 5, 1996 – Code of Conduct of the SBA for Securities Dealers of January 22, 1997 – Guidelines of the SBA for the Management of the Country Risk of September 4, 1997 – Agreement on the Swiss Banks Code of Conduct with Regard to the Exercise of Due Diligence of March 1, 1998 – Guidelines of the SBA for the Treatment of Dormant Assets of July 1, 2000 – Portfolio Management Agreement of July 24, 2000 – Code of Conduct of the Swiss Funds Association (SFA) for the Swiss Fund Business of August 30, 2000 – Guidelines on the calculation of net asset values and the handling of valuation errors in the case of securities funds as of 11 June 2001. In Switzerland, an entire set of reform projects is under discussion: – *Financial Market Supervision*: An Expert Commission instituted by the Swiss Finance

	Ministry issued a report and general recommendations regarding the reform of the framework for supervision of the financial sector. – *Bank Insolvency and Deposit Protection*: An Expert Commission instituted by the Swiss Finance Ministry put forward a proposal for an amendment to the Banking Act that includes provisions on the reorganization and liquidation of financial intermediaries, and mandatory deposit protection. – *Anti-Money Laundering*: The SFBC instituted a working group to review the Circular 98/1 on the Guidelines for the Combating and Prevention of Money Laundering of March 26, 1998 and the Agreement on the Swiss Banks Code of Conduct with Regard to the Exercise of Due Diligence of March 1, 1998. – *Supervision of Financial Conglomerates*: Proposal to codify the SFBC's practice regarding the supervision of financial groups and conglomerates in the Banking Act and SESTA (securities law). This may occur along with the amendment of the Act on the Supervision of Private Insurance. – *Auditing*: A working group mandated by the SFBC to review the legal framework for the auditing function presented a report with recommendations to further improve the system of bank auditing in Switzerland. Another working group is now in the process of drafting new regulations and amendments to existing regulations to implement the working group's recommendations. – *Code of Market Conduct*: The SFBC is currently in the process of drawing up a circular on a Code of Market Conduct, which further elaborates on terms such as market abuse and defines the legal concept of fair market conduct. – *Dormant Accounts*: Draft law awaits ratification by the Parliament. – *Implementation of the new Basel Capital Accord*: Steps of drafting appropriate instruments to transpose the new Accord into national law are taken. With regard to the additional criteria of the Core Principles Methodology, the findings are positive: The Banking Commission regularly reports to the Federal Council on its activities, at least on an annual basis. However, the Chairman and the senior management of the SFBC are not acting in plenary sessions of the parliament where all matters relating to supervision are presented by the Ministry of Finance. In general, the SFBC communicates with the Federal Council via the Federal Department of Finance. Under Art. 6 par. 1 of the Banking Act and title 7 of the Banking Ordinance, the SFBC has to ensure that all banks under its jurisdiction provide audited annual statements, including for their branches and representative offices. The Federal Council determines which banks are to prepare interim financial statements. Under Art. 6 par. 5 of the Banking Act the Federal Council sets forth the classification rules for a single company, consolidated and financial statements and lays down in which form and to which extent and within which deadlines they are to be published or made available to the public.
Assessment	Compliant.
Comments	
Principle 1(2)	Each such agency should possess operational independence and adequate resources.
Description	The SFBC has statutory independence in accomplishing its supervisory tasks (Art. 23 Banking Act). As a result of the meetings with the SFBC, there is no visible evidence of any government or industry interference in the work of the SFBC. The SFBC has adequate independence to deploy its banking supervision resources on its own. As stipulated in Art. 3 of the Banking Act, the SFBC is independent of all governmental agencies. It reports only to the Federal Council; it is not subordinated to the Government nor to any other executive institution of the State, which rules out active and ongoing intervention by Parliament or governmental bodies in pending matters. The accountability of the SFBC is performed on a strictly ex post basis, which rules out active and ongoing intervention by Parliament (or government) in pending matters. However, minor

	restrictions on the independence could exist insofar as the Federal Council and the Federal Department of Finance have the power to ask for reports on specific supervisory matters from the SFBC, voice their own opinion on supervisory issues and may criticize the SFBC in private or in public, which is in practice very rare. In addition, the parliament or the government could instruct or influence the work of the SFBC in abstract by adopting new legislation, where the SFBC is materially involved but does not have to agree on draft legislation. It is just possible that pressure may arise if there are differing opinions, for example, in the leading of the commission. As a result, there is no urgent need to extend the appointment of the present commission because the Chairman and the members of the SFBC are appointed only for a four-year terms. The Federal Council has the power to remove the commission only in the event of disciplinary misdemeanours or serious abuse of their functions. The SFBC has no budgetary independence, because it is part of the expense calculation of the central governments budget (2002: SwF 25,7 million). According to Art. 23 par. 4 of the Banking Act and the guidelines on the cost of the SFBC, the expenses are covered entirely by fees which were charged to Institutions under the supervision of the SFBC and not by the taxpayer. The salary policy of the SFBC is based on the labor market situation only to a minor extent, because the level of remuneration is subject to the terms for staff of the Swiss Administration in general and to the salary framework in particular. While the SFBC has to compete, for example, with banks for highly qualified staff, its ability to hire outside experts is limited by its own budgetary process. This causes problems to the expansion of supervisory responsibilities according to the new Basel Capital Accord. Most of the banks and banking associations which were interviewed by the members of the FSAP team would like to apply the internal rating approach (including cantonal banks and Raiffeisen banks; regional banks were indecisive). As a result of the ongoing dialogue with the Department of Finance, several improvements related to budgetary and human resources independence have been achieved: – Freedom to fix the number of staff within the limits of its budget. – A budget item under the title “enlarged supervision” presently amounting to 15 percent of the budget of the SFBC gives substantially more flexibility as it may be used for salaries as well as for indirect cost. – The SFBC is not included in the IT centralization exercise of the Swiss central administration (creation of a tailor-made system for the SFBC). – For recruiting and retaining of “selected” staff, the SFBC may grant a “labor market allowance” up to 20 percent on top of normal salary bands. This allowance needs to be approved by the Federal Department of Finance. The SFBC is presently exploring this possibility. The SFBC banking supervision staff has credibility based on their professionalism and integrity. This is expressed, for example, through the evaluation of Value-at-Risk (VaR) Models where statisticians and mathematicians are employed. The present supervisory strength is around 105 staff, with a core of about 75 persons having supervisory functions. In light of the expected increase in on-site visits and implementation of Basel II, the current staff level will be stretched or possibly insufficient regarding a staff turnover level of 18 percent in the year 2000. In order to offer a competitive and attractive position in the SFBC for highly qualified staff, the management of the SFBC is investing substantial resources in developing and enhancing the SFBC’s personnel management system. Its travel budget for on-site work allows appropriate supervision to be carried out on a consolidated basis. Improvement seems to be needed in the field of training, to maintain the high level of qualification of the staff. The system is based on the own initiative of employees.
Assessment	Largely compliant.
Comments	The SFBC has no budgetary independence, because it is part of the expense calculation of the central government’s budget. With regard to the proposal of the expert commission to establish an integrated financial supervision, recommendations aim to solve the identified problems.

Principle 1(3)	A suitable legal framework for banking supervision is also necessary, including provisions relating to authorization of banking establishments and their ongoing supervision.
Description	Under Art. 3 of the Banking Act and Art. 23 of the Banking Act, the SFBC is responsible for granting and withdrawing banking licenses. In order to organize and exercise supervision, the SFBC has the right under the Banking Act to issue regulations, guidelines and resolutions and to provide recommendations and explanations. This instrument is used quite often because amendments of the law involve an extremely time-consuming process in Switzerland. Art. 23 of the Banking Act gives the SFBC the right to demand additional information upon receipt, especially from the credit institution and shareholders who have qualifying holdings and companies belonging to the consolidation group in the form and frequency it deems necessary. In addition, the SFBC has the statutory duty and power to supervise state-owned banks (only by the Canton) in the same way as privately owned commercial banks. This includes the power to withdraw the state-owned banks' license and to close its business. The Federal Government does not own any bank.
Assessment	Compliant.
Comments	
Principle 1(4)	A suitable legal framework for banking supervision is also necessary, including powers to address compliance with laws, as well as safety and soundness concerns.
Description	Art. 23bis of the Banking Act enables the supervisor to address compliance with laws and the safety and soundness of the banks under its supervision. The Banking Act permits the supervisor to apply qualitative judgment in forming his opinion. The supervisor has unfettered access to banks' files in order to review compliance with internal rules and limits as well as external law and regulations. Based on this information, the SFBC is free to assess the evidence and to formulate its judgment with regard to compliance of the supervised institutions with law and regulations, and decides itself on whether and how to make use of its sanction powers. Art. 23 of the Banking Act enables the SFBC to take and/or require a bank to take remedial action. Furthermore, the SFBC can withdraw authorization if a credit institution violates the prudential rules established by or on the basis of the Banking Act/Banking Ordinance and, during the term specified, fails to return to compliance with those rules. The SFBC made use of this power about 30 times over the last 30 years. The most prominent closure of a bank concerned an insolvent medium-sized bank in 1991. However, the law does not specifically mandate when remedial action should occur. One reason is that the SFBC would like to react on a flexible basis, but such an authority is desirable for addressing problems at an early stage. The SFBC has the power and the duty to order a supervised institution to improve organizational shortcomings or correct breaches of prudential standards and it may also order specific changes. However, with regard to the depth of intervention, the SFBC applies restraint in order to avoid intervening in the business strategy of the supervised institution. It should be mentioned that, in conformity with continental Europe's system of administrative law, the SFBC itself has the power to issue formal enforceable decisions. It is possible to appeal these decisions to only one instance: the Swiss Federal Supreme Court, meaning only one level of appeal. The decisions of the SFBC may be challenged on the grounds of violations of law. However, the Federal Court does not review how the SFBC makes use of its discretionary powers if it did not abuse these powers in a qualified manner. The appeal has no suspension effect, but the court may grant a suspension. A formal decision issued and immediately executed by the SFBC may not be a ground for liability claims even if the decision has successfully been challenged in an appeal unless the SFBC has manifestly acted in bad faith.
Assessment	Compliant.
Comments	
Principle	A suitable legal framework for banking supervision is also necessary, including legal protection

1(5)	for supervisors.
Description	A protection process for the supervisory agency and its staff is in place. The staff of the SFBC may only be criminally prosecuted if the Federal Department of Justice and Police approves in conformity with Art. 15 of the State Responsibility Act 1958. The purpose of this provision is to protect civil servants against undue pressures exercised by unsubstantiated claims of alleged criminal acts. The approval is given based on an initial assessment of the evidence. If the Department of Justice and Police conclude that there is enough evidence to suspect a criminal offense it may deny approval only in cases of minor importance. At least for the last 25 years, there has been no criminal investigation against SFBC staff. No civil liability claim may be addressed directly against the members of the SFBC or its staff. Instead, claims have to be brought against the Swiss Confederation, which has to respond exclusively to all civil claims based on alleged breaches of statutory duties by the SFBC and its staff. In the last 20 years a handful of such lawsuits has been filed. All of them were dismissed by the Swiss Federal Supreme Court. If a civil servant has caused a loss intentionally or by gross negligence the Confederation has recourse against him. So far, no such recourse against a staff of the SFBC has ever been made.
Assessment	Compliant.
Comments	
Principle 1(6)	Arrangements for sharing information between supervisors and protecting the confidentiality of such information should be in place.
Description	An extensive process for exchanging information is in place between the SFBC and the Federal Office of Private Insurance, the other main supervisory authority in Switzerland. For the time being, the authorities see no need for a formal agreement. The Banking Commission may request information and documents from foreign banks and financial market supervisory authorities and has the authority to undertake direct inspections in foreign establishments of banks. A shortcoming could be that the exchange of information and on-site visits are in general based only on informal arrangements, since a large part of the business of the two largest Swiss banks is established in the United States and the United Kingdom. However, such informal arrangements have not impaired the SFBC's ability to practice consolidated supervision, including on-site inspections if necessary. Several exchanges of letters on cooperation and information sharing have been agreed upon; for example, with the Netherlands. Under Art. 7 of the Banking Act the banks shall submit their annual financial statements to the Swiss National Bank (SNB). With regard to the cooperation with the SFBC, the Act on the Swiss National Bank is expected to be amended. The SFBC, according to Art. 23 ^{sexies} par. 2, may only transmit information and documents disclosing confidential information to foreign banks and financial market supervisory authorities if these entities: – will use information for direct supervision; – are bound by official or professional secrecy, and – "will not transmit this information to competent authorities or bodies which are entrusted with supervisory activities in the public interest without the prior consent of the Banking Commission or on the basis of a blanket permission contained in a treaty with a contracting state. The transmission of information to penal authorities is not permitted whenever legal assistance in penal matters would be excluded. The Banking Commission decides after consulting with the Federal Office of the Police." Information on individual customers will not be transmitted by the SFBC without their approval.
Assessment	Compliant.
Comments	The exchange of information and on-site visits are generally based on informal arrangements. In light of the key importance of exchange of information among supervisors in the case of large and

	complex financial institutions, more formal arrangements should be considered.
Principle 2.	**Permissible Activities** The permissible activities of institutions that are licensed and subject to supervision as banks must be clearly defined, and the use of the word "bank" in names should be controlled as far as possible.
Description	The term bank is clearly defined under Art. 1 of the Banking Act. Under Art. 2a of the Banking Ordinance a credit institution is a company whose principal and permanent activity is to receive cash deposits and to grant loans for its own account and provide other financing. Neither the Banking Act nor the Banking Ordinance lists in detail the transactions and actions that are permissible for credit institutions including those that are directly ancillary or supplemental to its principal activity. Other core banking activities such as payment systems are not identified as banking activities as they are, for example, in the EU. This type of business could especially be a cause of systemic risk to the financial system. Only credit institutions are allowed to use the term "bank" or "banker." These terms, alone or in combination with other words, may only be used in the company name, designation of the business purpose or advertising if the institutions concerned have obtained a license from the SFBC. In general, credit institutions have the exclusive right to receive money from the public for the purpose of depositing or receiving repayable funds in any other manner, according to Art. 1 par. 2 of the Banking Act. However, this particular section of the law says that the Federal Council provides for exceptions as long as the protection of the depositors is assured (clarified through circular 96/4). As a result, monies of employees as well as retired employees with their employer (e.g., industrial companies) are not considered as deposits and not subject to licensing and supervision by the SFBC. Such an exception poses a systemic vulnerability since the bankruptcy of a commercial company could result in the loss of their employees and retirees deposits. A current example is the recent bankruptcy of Swiss Air and its deposit-taking entity which required rescuing in the amount of SwF 110 million. The SFBC does not know how many of these deposit-taking entities exist, or their size. This could be a cause of systemic vulnerability if there is an unknown segment of the financial sector that is unregulated.
Assessment	Largely compliant.
Comments	Credit institutions do not have the exclusive right to receive money from the public for the purpose of depositing or receiving repayable funds in any other manner. An exception in the Banking Act (Art. 1 par. 2) permits nonbank employer sponsored deposit-taking entities that are not licensed or regulated as financial institutions. This poses a risk to the system.
Principle 3.	**Licensing Criteria** The licensing authority must have the right to set criteria and reject applications for establishments that do not meet the standards set. The licensing process, at a minimum, should consist of an assessment of the banking organization's ownership structure, directors and senior management, its operating plan and internal controls, and its projected financial condition, including its capital base; where the proposed owner or parent organization is a foreign bank, the prior consent of its home country supervisor should be obtained.
Description	Prior to engaging in banking activities in Switzerland, each institution must obtain a license from the SFBC (Art. 3 of the Banking Act), which is the sole and independent authority for granting banking licenses. A Swiss banking license is considered a universal bank license which is not limited to specialized business fields, such as commercial, investment, and private banking. The regulations governing the acquisition of an existing bank basically parallel those governing its initial establishment. The SFBC's licensing guidance and practice are consistent with those of the EU's Second Banking Directive on Licensing and Supervision of Credit Institutions. In its implementation, every credit institution is required to manage its business in accordance with sound administrative principles and to put in place and maintain internal controls and reporting arrangements and procedures to ensure

	that the business is so managed. Art. 3 of the Banking Act specified in title 2 and 3 of the Banking Ordinance provides the criteria for issuing licenses consistent with those applied in ongoing supervision. Art. 23 of the Banking Act gives the SFBC the right to reject applications if the criteria are not fulfilled or if the information provided is inadequate. The reasons for negative decisions regarding license applications have mainly been the lack of qualified banking skills and experienced staff and thus an organization or management not adequate or competent enough for the planned activities. The SFBC has published a Guideline for License Applications for Banks and Securities Dealer (21.9.1999), which is not legally binding. The Banking Act read in conjunction with the Banking Ordinance enables the SFBC to determine that the proposed legal and managerial structures of the bank will not hinder effective supervision. Art. 3 of the Banking Act in conjunction with title 2 and 3 of the Banking Ordinance helps the SFBC to determine the suitability of major shareholders, transparency of ownership structure and source of initial capital. Art. 3 par. 2c of the Banking Act / Art. 6 of the Banking Ordinance and the above-mentioned guideline set forth the evaluation criteria for the SFBC regarding the fitness and propriety (education, experience and professional qualification, and trustworthiness) of the proposed bank managers. Directors and managers of the bank must be competent and fit for the specific business of the new bank, that is, their personal integrity and professional skill as well as their experience must meet the demands of their new task. All license applications must include the curricula vitae of key personnel, extracts of the general registry of criminal records (where available), and references for all directors and senior management. This procedure applies also to shareholders who wish to acquire a qualifying holding. They have to guarantee that their influence will not have a negative impact on a prudent and solid business activity. The qualified shareholders and the banks have a legal duty to report the relevant shareholdings and their changes to the SFBC. The SFBC is entitled to enforce the "fit and proper" requirement by suspending the voting rights of non-complying shareholders up to revoking the banking license in severe cases. Apart from this qualitative requirement, the banking legislation applies no quantitative limitation on ownership in banks. Art. 4 par. 1 of the Banking Ordinance requires that the new bank must have a paid-in capital of at least SwF 10 million. In cases where, according to the business plan, the projected activity requires more funds—which is normally the case—the initial capital can go up to SwF 20 million or more. Title 2 of the Banking Act and title 2 of the Banking Ordinance require and provide for a detailed review of procedures on corporate governance, strategic and operating plans, structure and policies and procedures, internal control procedures and system for appropriate oversight of the credit institution's activities in the proposed credit institution. This means that the bank to be licensed has to set up an organization that is able to meet the demands of the projected business. In this regard, its by-laws and internal regulations have to clearly define the type and geographical limits of the planned banking activity and, accordingly, the internal organization for that activity. Furthermore, the bank's responsibilities and the internal control procedures have to be adequately described. The SFBC not only formally approves the by-laws and internal regulations on the occasion of the establishment of the bank, but also their subsequent changes and amendments. Within the organization of the new bank there must be a separation between the supervisory and policy-making functions of the board of directors and the executive function of the management (Art. 8 par. 2BO). The same individual must not serve on both bodies. The Banking Act and Banking Ordinance contain detailed guidelines concerning the documents to accompany the authorization application, that is, the pro forma financial statement and the financial information on the principal shareholders. The SFBC grants authorization if, in the opinion of the supervisors, the business plan of the credit institution being founded is feasible and the above-noted criteria are met. According to Art. 3^{bis} of the Banking Act, the consent of the banking supervisory authority of the home country of the credit institution is required prior to the foundation or acquisition of a

	subsidiary credit institution or the foundation of a branch in Switzerland. If a financial conglomerate or banking group owns the foreign bank, a declaration of the home-country authority that it supervises the conglomerate/group on a consolidated basis is needed. The firms or bank name should not indicate or suggest a Swiss character. The reciprocity requirement, which is also mentioned in the law, has lost its importance due to Switzerland's adherence to GATS (General Agreement on Trade and Services), which requires Switzerland to apply the most-favored-nation-rule to all WTO members. Under Art. 23 ^{quinquies} of the Banking Act, the SFBC has the opportunity to revoke a license if it determines that the license was knowingly based on false information. Art. 46 par.1.i of the Banking Act gives the SFBC the power to discipline bank management if incorrect information has been furnished to the SFBC. From 1996 to 2000, the SFBC granted 70 banking licenses (branches of foreign banks included). Forty-five licenses concerned entities under foreign ownership (including 23 branches of foreign banks) and 25 entities were in Swiss hands. The 70 new institutions focus predominantly on private banking. In the period from 1991 to 2000, a total of 243 banking institutions ceased their banking activity. Three of those faced the withdrawal of their banking license from the SFBC, 182 surrendered their license in the course of mergers and 58 went into liquidation. The total assets of the mentioned 243 banking entities amount to SwF 140 billion.
Assessment	Compliant.
Comments	In granting 70 banking licenses (branches of foreign banks included) over the past five years, SFBC's main focus has been on private banking.
Principle 4.	**Ownership** Banking supervisors must have the authority to review and reject any proposals to transfer significant ownership or controlling interests in existing banks to other parties.
Description	A direct or indirect holding in a bank which represents 10 per cent or more of the share capital or votes in the bank, or a significant influence in the bank's business activities in another manner, is deemed to be a qualifying holding (Art. 3 par. 2c$^{bis13\ 14}$ of the Banking Act). Prior authorization is required for a person seeking to acquire a qualifying holding in a bank or to increase a qualifying holding so that the proportion of the share capital or votes in the bank held by that person exceeds 20, 33, 50 percent or a percentage that allowed the bank to become controlled by that individual. The Banking Act gives the SFBC the right to grant authorization for the acquisition and the right to require notification in the case of an increase of qualifying holding (Art. 3 par. 5 of the Banking Act). The SFBC is entitled to enforce the "fit and proper" requirement by suspending the voting rights of non-complying shareholders up to revoking the banking license in severe cases. The authorization can also be withdrawn if, for example, the activities of the shareholder cause a significant risk to the sound and prudent management of the credit institution (Art. 23 par.1ter and ^{quinquies} of the Banking Act). Apart from this qualitative requirement, the banking legislation applies no quantitative limitation on ownership in banks. According to Art. 3 par 6 of the Banking Act and Art. 6a of the Banking Ordinance, a credit institution has to submit to the SFBC a list of shareholders of which it has knowledge, at least annually. Changes of qualified holdings must be immediately reported to the SFBC.
Assessment	Compliant.
Comments	
Principle 5.	**Investment Criteria** Banking supervisors must have the authority to establish criteria for reviewing major acquisitions or investments by a bank and ensuring that corporate affiliations or structures do not expose the bank to undue risks or hinder effective supervision.
Description	Generally, Swiss banking law imposes no specific structural conditions or restrictions on banks engaging in securities activities, real estate or insurance business.

	According to Art. 4 par. 2[bis] of the Banking Act, a qualifying holding in any other company held by a credit institution or by a company belonging to the same consolidation group shall not exceed 15 percent of the net own funds of the credit institution or the consolidation group thereof, respectively. Furthermore, the total amount of investments in the financial fixed assets (shares, debt instruments and other securities, acquired for use on a continuing basis and for gaining profit during an extended period) of other companies shall not exceed 60 per cent of the net own funds of the credit institution or the consolidation group. Art. 4bis par. 1 of the Banking Act requires that investments in a single company should have an adequate relation to their own funds. The investments in industrial equity have to be covered by capital equal to 40 percent (500 percent risk weighting for capital adequacy requirements) of the investment. This is the reason why Swiss banks own comparatively small industrial equity portfolios.
Assessment	Compliant.
Comments	
Principle 6.	**Capital Adequacy** Banking supervisors must set minimum capital adequacy requirements for banks that reflect the risks that the bank undertakes, and must define the components of capital, bearing in mind its ability to absorb losses. For internationally active banks, these requirements must not be less than those established in the Basel Capital Accord.
Description	The Banking Act and Banking Ordinance along with circulars: – EBK-RS 97/1 (market risk) – EBK-99/1 (interest rate risk) vested in it under that legislation, apply to all banks operating within Switzerland. The principles applicable to banks, together with capital requirements for banks lay down in Art. 4 of the Banking Act and title 4 of the Banking Ordinance. The provisions contained a specification of: – the components and structure of bank capital – the equity requirements – the deductions from required equity The regulation applied in Switzerland regarding the definition and structure of a bank's capital base and the regulation on capital adequacy is in line with the 1988 Capital Accord of the Basel Committee on Banking Supervision and is close to the EU directives on Own Funds and Solvency. The amendments to the above-mentioned Capital Accord are covered, especially on market risk. In general, each Swiss bank has to fulfill the same capital requirements. Branching within Switzerland is not subject to any legal additional capital requirements. Art. 4 of the Banking Ordinance Act stipulates that the paid-in share capital of a bank to be established shall be at least SwF 10 million. Initial disbursements of capital cannot be made, either with subordinated debt or with other funds borrowed by the bank itself. As far as the shareholders are concerned, the SFBC verifies their identity and sound financial standing as items of the license application in the authorization process. Art 4 par. 1 of the Banking Act requires that banks must provide for an adequate relationship between: – their equity and their total liabilities; – their liquid assets and their easily marketable assets on the one hand, and their short-term liabilities on the other. The Banking Ordinance establishes the directives to be observed in this respect under normal circumstances, taking into consideration the kind of business and the type of bank. It shall define the terms of the own funds, liquid assets, easily marketable assets and short-term liabilities (Art. 4 par. 2 of the Banking Act).

	The definition of capital is consistent with the Basel Capital Accord. Art. 11 of the Banking Ordinance define the components of capital. On the equity requirements Art. 12 of the Banking Ordinance requires all banks to calculate and to maintain a minimum capital adequacy ratio no less than 8 percent, reduced by existing value adjustments and provisions. The SFBC requires a higher rate of capital adequacy. Based on this, the capital adequacy ratio was raised to a minimum of 10 per cent. The SFBC sees higher capital as giving a competitive advantage and also fostering the good reputation of the Swiss financial market. The definition of capital, method of calculation, and the ratio required are more stringent than those established in the Basel Capital Accord. The resulting capital charge is a function of the structure of the risk-weighted assets, the calculation method used (standardized approach, internal risk aggregation model approach), and of the individual positions. In general the capital requirements reflecting market risks are consistent with the Basel Capital Accord. Minor differences exist for the following: – foreign exchange risk and gold positions, for which the capital charge is 10 percent (instead of 8 percent); – commodity risk, for which the capital charge is 20 percent (however, with a simpler approach); – equity risk, for which, for the purpose of calculating the general market risk, a net position per domestic equity market or per single currency zone can be calculated. Under Art. 13a of the Banking Ordinance capital adequacy ratios are to be calculated on both a consolidated and a solo basis for the banking entities within a banking group. Art. 12 a and b of the Banking Ordinance covers both on and off-balance-sheet items. According to Art. 13b of the Banking Ordinance banks must report their capital adequacy ratio on a solo basis quarterly and the capital adequacy ratio on a consolidated basis half yearly. As a result, the implementation of the Basel Capital Accord in Swiss banking legislation is more risk adequate because of more differentiated and tighter risk weightings. However, the risk weightings on receivables directly or indirectly secured by mortgages must be weighted with 75 percent (Basel: 100 percent). Art. 13b of the Banking Ordinance factors in the cantonal guarantees for liabilities provided for their banks and allows a capital discount of 12.5 percent of required equity for cantonal banks. This is the only significant remaining difference in prudential treatment between these banks and the other Swiss banks. The discount is no longer necessary and should be eliminated to provide a level playing field between the cantonal and other Swiss banks. The SFBC must be informed immediately whenever capital requirements are not met. Under Art. 23 of the Banking Act as a general provision, the SFBC has the right to enforce sanctions for violations of the provisions of the Banking Ordinance on capital adequacy. However there are no indicative benchmarks for triggering action on inadequate capital adequacy. As part of the licensing process the Banking Act requires that a credit institution and the companies belonging to a consolidation group have systems and strategies for risk monitoring, risk management and risk assessment, which are appropriate and sufficient for their activities. They must also have internal rules, which are subject to review and updating on a regular basis, that apply both to the credit institution and companies belonging to the same consolidation group. Capital adequacy rules are also applicable to all banking affiliates of Swiss banks whether domestic or foreign. The capital adequacy requirements are not applicable to Swiss branches of foreign banks. According to the current position of the SFBC, it is up to the bank supervisory authority of the home country to monitor the bank's consolidated equity position properly.
Assessment	Compliant.
Comments	Capital requirements are more conservative than the Basel Capital Accord. Nonetheless, for the large and systemically important financial institutions, frequent and close monitoring of the capital position is recommended due to their often complex activities and possibly rapid changes in risk profiles. The 12.5 percent capital reduction for cantonal banks should be eliminated.

Principle 7.	**Credit Policies** An essential part of any supervisory system is the independent evaluation of a bank's policies, practices, and procedures related to the granting of loans and making of investments and the ongoing management of the loan and investment portfolios.
Description	Art. 3, 2a of the Banking Act states that a license will be granted if: " the articles of association, by-laws, company contracts and business rules of the bank provide for a clear definition of the scope of business and establish an adequate organization corresponding to the proposed business activities; where the scope or the importance of the business activities is significant, the bank must create separate bodies for the management on the one hand and for the direction, supervision and control on the other. The authorities of these bodies must be segregated in a manner so as to ensure the effective supervision of the bank's management." Subsequent audits confirm such prudential requirements continue to exist after the bank commences business. The large risks are risk-weighted and must be reported when attaining or exceeding 10 percent of the banks eligible equity resources. Reporting of the large risks to the external audit firm is required once every three months. The ten largest debtors (not risk-weighted) must be included once a year in the long-form report. Not included are receivables, which are secured by movable assets traded on a recognized stock exchange or a representative market as defined in Art. 14.d of the Banking Ordinance and which are customarily accepted by banks, fiduciary deposits or cash deposits as well as debtors that are public-law corporations in OECD countries or domestic and foreign banks and securities dealers. In general, the SFBC enjoys considerable discretion within the framework of the Banking Act when granting licenses. The Banking Ordinance details the prudential requirements applicable to bank lending in Art. 9, "The bank shall lay down in regulations or in internal guidelines the main principles underlying the management of risks and the competencies and procedures for the approval of risk transactions. It must in particular identify, limit and supervise market, credit, default, settlement, liquidity and image risks as well as operational and legal risks." Each bank is required to have appropriate policies relating to the management and control of lending that include credit assessment, credit review, risk management, the monitoring and control of large exposures and prudent provisioning for loan losses. Limits of lending officers must be incorporated in a bank's internal regulations and any changes to the internal regulations require notification to and approval of the SFBC (Art. 9 of the Banking Ordinance and also Art. 3 par 3 of the Banking Act). Art. 19 par. 1 and Art. 21 par. 1 of the Banking Act and SFBC-Circular 96/3 cover the requirements for auditors (authorized by the SFBC) inspection/ verification activities for lending. External auditors are charged with assessing a bank's loan and investment portfolios within the context of their annual bank audit and must attest to compliance with all SFBC issued rules relating to granting loans and making investments and ongoing management of these assets. External auditors follow detailed audit procedures in approved audit manuals which also include sampling loans, including those noted on a bank's internal watch list and those included in internal loan classifications. A sample of recently granted credits is reviewed for adherence to internal bank policies and practices. The SFBC also identifies one "specialized" supervisory area each year for the external auditors to focus on during their audits and the credit area periodically receives special attention in this way. *Regarding investment criteria*: The SFBC requires, and authorized external auditors periodically verify, that prudent investment criteria, policies, practices and procedures are approved, implemented and periodically reviewed by bank management and boards of directors. The SFBC supervises banks' investment activities via oversight of the work of the external auditors both in the context of market and credit risk as detailed in the Banking Ordinance, Section 6 on Risk Diversification, Art. 21 and 22, SFBC-Circular 96/3 (Audit Report: Form and Contents) and SFBC-Circular 97/1 (Guidelines on Capital Adequacy Requirements to support market risks of Art. 12 par. l-12p of the Banking Ordinance). Debt securities and equity shares held as financial fixed assets are normally held for the purpose of "structural" balance sheet management, and positions are reviewed during on-site inspections by the external auditors. Such positions are part of a bank's investment and funding activities in the money market, capital market and derivatives markets.

	Investments, like loans, are extensions of credit involving risks that carry commensurate rewards. The SFBC expects risks in the investment portfolio to be minimized in order to maintain adequate liquidity and marketability. The associated risks (i.e., interest rate, liquidity and foreign exchange, if applicable) are usually monitored and controlled by a bank's Asset and Liability Committee (ALCO) or Risk Committee within established policy and limits approved by the Board of Directors. Such investments should be included within a bank's internal liquidity report for management. External auditors review such investments and how they are used by a bank using procedures in approved auditing manuals. The credit quality of investment securities is monitored through credit analysis, emphasizing a review of current financial information and the use of approved rating agencies. SFBC-Circular 98/3 contains a list of recognized rating agencies. In the larger banks counterparty risk is usually monitored and controlled by a bank's Credit Committee or loan officers within policy and limits approved by the Board of Directors. The external auditors check to see that both the ALCO and the Credit Committee operate independently of the business units taking the risk. Examiners (on an indirect basis) and external auditors (directly) determine that the performance and quality of investments are monitored frequently and subject to regular reporting to Senior Management and the Board of Directors. Compliance with policy guidelines, particularly valuation of investments, is assured through adequate internal controls, internal and external audit coverage and review. *General:* The credit risk environment is set via established policies and procedures required of banks by the SFBC in the initial licensing business plans. Such policies and procedures are checked annually by external auditors. The SFBC defines credits overdue 90 days or more as "impaired." However, no data is collected by the SFBC regarding renegotiated, past due and internally classified credits. Such information, along with provisions, chargeoffs and recoveries, is considered useful in monitoring asset quality trends in the banking system. Although the SFBC has not specifically adopted an asset grading/classification system that all banks must adopt, the SFBC requires that credit institutions have an internal loan classification system in place and external auditors look at any classified, reclassified, or rescheduled loans during their annual audits. Auditors also sample denied loans. The SFBC defines impaired and non-accrual status credits for reporting purposes but leaves internal loan classifications up to management to decide and the external auditors to assess. SFBC-Circular 95/1 (Internal Audit) does not include specific reference to adequate controls over credit risk, per se, but broadly covers this area. In addition, a bank's investment policies, practices, and procedures are usually inspected as part of the external auditor's annual bank audit of credit risk and market risk. Specialized inspections by external auditors of investment activities may also be conducted if the SFBC determines a bank's investment activities are material and such inspection is warranted. All loans to bank insiders are required to be extended at an arm's length basis with no or minimal discounts below current market rates allowed. Specific limits in relation to credits granted to directors, significant shareholders and businesses where the bank is a shareholder are not set by the SFBC but rather determined by the individual banks and then checked by the external auditors during their on-site audit. While there are no statutory limits regarding loans to affiliates, "firewalls" are generally imposed regarding lending to affiliates of a bank, which are part of a commercial/industrial group (per Art. 4ter of the Banking Act). The external audit procedures cover reviewing loan policies to ensure they address loans to directors/major shareholders and connected entities. Detailed verification procedures regarding such credits broadly cover conflicts of interest arising in the conduct of different types of activity (such as credit) and require an institution to satisfy the external auditor regarding arrangements made to protect interests of a bank's clients. The SFBC requires that such arrangements should include arms-length transactions and credit granted based on sound underwriting criteria, free from outside pressures. Art. 9 par. 2 of the Banking Ordinance requires appropriate policies and procedures relating to management and control of lending. As part of the annual external audit process, SFBC staff

	determines adherence to policies and procedures. In order to comply with the policies and procedures for granting credit, the credit institution must ensure the policies are communicated to employees and that appropriate procedures are followed. SFBC circulars (cited above) address procedures used for assessing underwriting standards and credit granting criteria. Art. 3 of the Banking Act and Art. 9 of the Banking Ordinance requires credit institutions have in place such committees of directors and management as are necessary to ensure that the business of the credit institution is being managed, conducted and controlled in a prudent manner and in accordance with sound administrative principles. Thus, in order to comply with this requirement, a credit institution must have a loan or credit committee that is responsible for approving credits of significant monetary amount or above a certain risk level and appropriate policies relating to the management and control of lending. External auditors must assess and attest to the adequacy of an institution's written lending policies and procedures, including the duties and responsibilities of loan officers and loan committees and loan approval limits, during annual audits. Art. 9 of the Banking Ordinance requires that comprehensive risk management systems commensurate with the scope, size and complexity of all the credit institution's activities be in place, incorporating continuous measuring, monitoring and controlling of risk, accurate and reliable management information systems, and timely management reporting. Such management information systems (MIS) should provide essential details on the condition of the loan and investment portfolios if banks are to comply with the SFBC's Banking Ordinance. Compliance is checked during on-site audits by the external auditor. Art. 21 of the Banking Ordinance requires monitoring and control of large exposures. The Banking Ordinance is consistent with the EC Directive on Monitoring and Control of Large Exposures (92/121/EEC). The Banking Ordinance requires credit institutions to have administrative, accounting, and control mechanisms in place for identifying, and recording all large exposures and any changes to them. The SFBC monitors and the external auditors verify compliance with large exposures on a consolidated basis. There are credit reference agencies/credit bureaus that collect data on lending by different institutions to individual borrowers. In addition, external auditors review a sample of loans during their on-site audits. In order to monitor capital, loan loss provisions and impaired loans as required to be reported to the SFBC semi-annually for the majority of banks, bank management must monitor their credits on a regular basis.
Assessment	Compliant.
Comments	No data is collected by the SFBC regarding renegotiated, past due and internally classified credits. Such information, along with provisions, chargeoffs and recoveries, is considered useful in monitoring asset quality trends in the banking system.
Principle 8.	**Loan Evaluation and Loan-Loss Provisioning** Banking supervisors must be satisfied that banks establish and adhere to adequate policies, practices, and procedures for evaluating the quality of assets and the adequacy of loan-loss provisions and reserves.
Description	All banks are required to establish a risk management program and set forth the main principles of the program in approved policies. Such policies must pay particular attention to credit risks and define lending limits, credit assessment methods, large exposures, country risks, etc. The SFBC approves credit policies at the time of licensing and the external auditor reviews the policy annually for compliance (Art. 9 par. 2 of the Banking Ordinance). The bank’s internal audit function audits compliance with the policies and procedures and submits reports on the credit risk area directly to the board of directors and to the SFBC if required to do so or material issues are detected. These reports are also made available to the external auditor. The external auditing firms have to assess compliance with the policies and procedures and provide comments in their audit reports to the SFBC (Art. 43-49 of the Banking Ordinance). The external auditors must also independently value the assets and liabilities based on the bank’s documents and records (Art. 43 par. 3 of the Banking Ordinance).

	Identified risks must be fully provisioned. The risk evaluation has to be based on a complete and current documentation that allows an assessment of the present value of any collateral or demonstration of collateral deficiency. If the documentation is not complete or not available, the loan must be designated as totally impaired (and valued at "0"), which requires full provisioning. If the provisioning is insufficient, the auditor will instruct the bank to increase the amount of the provision. If the bank fails to increase the provision as directed by the auditor, the auditor must report this failure to the SFBC. The SFBC receives annually information from the external auditor on a bank's loan portfolio, internal rating system, provisioning amounts, etc. There is no legal requirement that specifies a particular credit classification category for non-accrual loans. According to the principle of safe and sound banking, banks must provide for specific provisioning for that part of a loan, which is or may become a loss, taking into consideration the existing collateral. A loan is classified as impaired after 90 days but placing a loan on non-accrual status is a management decision. Each bank uses its own rating system and the time criterion to assign a loan into a substandard class is not the sole basis for classification (collateralized loans may not be downgraded if there is adequate collateral to cover the interest and the principal). In case of inadequate collateral or unsecured loans, a loan 90 days past due is considered impaired. There are no minimal provisioning requirements for standard loans. Banks must transfer a least 5 percent of their yearly net profits into the general reserve as long as this reserve does not reach 20 percent of the paid-in capital (Art. 5 par. 1 and 1^{bis} of the Banking Act). Off-balance sheet positions are valued and provided for in the same way as the on-balance sheet positions when defining the credit and default risks and required provisioning. The SFBC requires banks to submit their accounts according to the principles of orderly bookkeeping and in such a manner as to permit the most reliable possible assessment of the net assets (Art. 24 par. 1 of the Banking Ordinance). Banks must publish their annual financial statements (Art. 26 par. 1 and 2 of the Banking Ordinance) and ones with a balance sheet total over SwF100 million must establish interim accounts on a half-yearly basis (Art. 23b par. 1 of the Banking Ordinance). Copies of these statements must also be submitted to the SFBC (Art. 26 par. 4 of the Banking Ordinance). Asset quality must be reviewed at least on a yearly, if not a half-yearly, basis. As noted in the assessment of CP 7, additional asset quality data, on a more frequent basis (such as quarterly) should be obtained by the SFBC and used in monitoring any deteriorating trends in asset quality. Nonperforming loans are defined as loans to customers and mortgage loans the interest payments of which have become overdue. There is a presumption that interest and commissions more than 90 days overdue are a loss. In the case of current accounts, the presumption applies when the overdraft limit is exceeded for more than 90 days. If the recovery of the interest is also at risk, it is also considered a loss and should be written off, even if the credit is less than 90 days overdue. If a credit is 90 days overdue but remains on the bank's books, it will cease accruing interest and commissions. Interest and commissions are either credited to value adjustments and provisions, or cease to be accrued altogether. Interest and commissions already accounted for as income shall not be reversed, but shall be included in a bank's provision (see also Reporting Guidelines No. 106). Any accounting treatment that diverges from the above must be described in the notes to financial statements (pursuant to Art. 25c par. 1 ch. 2 of the Banking Ordinance, Guidelines of the Federal Banking Commission concerning the provisions governing financial statement reporting RRV-SFBC *"Reporting Guidelines," No. 106*). Accrued, though unpaid, interests are recorded as interest income as long as the loan is performing (full accrual accounting, Art. 24 par. 2 lit. h of the Banking Ordinance). The book value of nonperforming loans must be disclosed annually to the SNB and the SFBC (SFBC- Circular 99/3, and SNB Form "FI03/23"). The audit firm's review annually compliance with accounting and prudential requirements (Art. 19 par. 1 of the Banking Act) and report to the SFBC (Art. 21 par. 1 of the Banking Act, Art. 43^{ss} of the Banking Ordinance). Based on information received from the audit firm or other sources indicating potential violations of valuation rules, the SFBC may take several actions: – request additional information from the bank, the audit firm, or both (Art. 23^{bis} par. 2 of the

	Banking Act); – request an extraordinary review to be performed by an independent audit firm (Art. 23bis par. 2 of the Banking Act); – request the bank present draft financial statements in the future to the SFBC before publication; – demand corrections to the financial statements, including an increase of value adjustments and provisions, if the investigations confirm that they are substantially understated and republish if necessary (Art. 23ter par. 1 of the Banking Act); – require modification of inappropriate accounting policies or valuation criteria (Art. 23ter par. 1 of the Banking Act). The SFBC may also command reinforcement of capital requirements (see Art. 4 par. 3 of the Banking Act), effectively reducing the credit activity of the bank. *Financial statements* must be made available to the public (Art. 6 par. 4 of the Banking Act. Also see CP 21). Financial statements include information relevant to loan classification and provisioning including Segmentation of loans by counterparty (per Reporting Guidelines); Disclosure of loans to related parties (per Art. 25 par. 1 ch.1.13.2 and 25c par. 1 ch. 3.13 of the Banking Ordinance); Disclosure of off-balance sheet operations (per Art. 25 par. 1 ch. 3 of the Banking Ordinance, Reporting Guidelines No. 93 to 102); Further segmentations are to be disclosed in the notes to financial statements (Art. 25c par. 1 ch. 4 of the Banking Ordinance, Reporting Guidelines No. 191 to 198); Segmentation of loans by collateral at market value (per Art. 25c par. 1 ch. 3.1 of the Banking Ordinance, Reporting Guidelines No. 150 to 153); Disclosure of movements in provisions (Art. 25c par. 1 ch. 3.9 of the Banking Ordinance, Reporting Guidelines No. 169 to 173); Segmentation of assets by maturity, country, and currency (Art. 25c par. 1 ch. 3.12, 3.14, 3.15 and 3.16 of the Banking Ordinance, Reporting Guidelines No. 177 to 190). *Prudential reporting* covers reporting large risk exposures (per Art. 21 ss of the Banking Ordinance). Credit risk supervision (per SFBC-Circular 96/3 Cm 16) includes assessing, at least annually by the external auditor, the internal control system of the bank regarding credit risk. The assessment is included in the Long Form report (see CP 21) and must include, at a minimum: the credit granting and monitoring process; the treatment of loans to bank management and Board Members and important shareholders (per Art. 4ter of the Banking Act); the appropriateness of risk measurement methodologies; the appropriateness of value adjustments and provisions; and internal reporting to the management and the board of directors. Prudential reporting in the credit area also must address the tax impact of loan loss provisions (per Art. 57, Art. 63 par. 1 of the Federal Income Tax Act (LIFD, RS 642.11), Art. 24 par. 1 and 4, Art. 10 par. 1 of the Federal Income Tax Harmonization Act (LHID, RS 642.14)). Provisions that have ceased to be economically justified are part of the taxable income (Art. 63 par. 2 LIFD, Art. 24 (1) LHID), whether or not they were actually released to the income statement. The Banking Act, Banking Ordinance and SFBC Guidelines have established a clear, general reporting and credit classification framework. They require Swiss banks to formulate specific policies for identifying and dealing with problem credits including procedures to ensure that classifications, loan loss provisions and write-offs reflect realistic repayment expectations. The classification and provisioning policies of a bank and their implementation are regularly reviewed by the banks' internal and external auditors and the SFBC. The external auditors and the SFBC via review of the external audit reports determines that banks have appropriate procedures and organizational resources for the ongoing oversight of problem credits and for collecting past due loans. The SFBC also has the authority to require a bank to strengthen its lending practices, credit-granting standards, level of provisions and reserves, and overall financial strength if it deems the level of problem assets is too high. The SFBC is generally informed annually or semi-annually in reports filed by the banks concerning the classification of credits and assets and provision amounts. If a bank is a problem bank or one of the two large banks, more frequent reporting is received (i.e., monthly or quarterly).

Assessment	Compliant.
Comments	
Principle 9.	**Large Exposure Limits** Banking supervisors must be satisfied that banks have management information systems that enable management to identify concentrations within the portfolio, and supervisors must set prudential limits to restrict bank exposures to single borrowers or groups of related borrowers.
Description	See CP 8. The Swiss risk diversification rules are modelled on those of the BIS as well as those prevailing within the European Union in the EC Directive on the Monitoring and Control of Large Exposures of Credit Institutions (92/121/EEC). Risk diversification rules are set forth in Art. 21 and 22 of the Banking Ordinance. With the exception of Swiss branches of foreign banks, all banks must comply with these rules on an individual company as well as on a consolidated basis if the equity capital requirements are to be complied with on a consolidated basis. The limitation of risk concentrations occurs on three levels: – The first limit of 10 percent of the institution's eligible capital turns a risk position into a risk concentration in so far as it is reached or exceeded (Art. 21 par. 1 of the Banking Ordinance). This risk concentration, although in principle is authorized in this size, must be reported to the bank's board of directors as well as to the external auditors on a quarterly basis and, at least, on an annual basis to the SFBC. – In addition, there is an upper limit of 25 percent of the institution's eligible capital, which the risk position of a counterparty may not exceed (Art. 21a par. 1 of the Banking Ordinance). – Subject to certain exceptions, the aggregate amount of all large exposures must not exceed 800 percent of the bank's eligible capital (Art. 21b par. 1 of the Banking Ordinance). A risk position may exceed these limits if the excess is covered by freely eligible capital (Art. 21a par. 5 of the Banking Ordinance). An allocation of this nature of freely eligible equity resources must be disclosed in the quarterly computation of required equity submitted to the Swiss National Bank (SNB). The risk position of each single counterparty or connected group of counterparties (according to Art. 21c par. 1 of the Banking Ordinance, related counterparties are considered as a unit) comprises all outstanding positions, off-balance sheet transactions and net long positions in securities which are risk weighted pursuant to the general rules on capital requirements (Art. 21d par. 1 of the Banking Ordinance). Off-balance sheet transactions are converted into their credit equivalent before being added to the risk position. Intra-group transactions may not be subject to the usual rules if the whole group and the group company concerned are supervised on a consolidated and individual basis that is considered to be appropriate (Art. 21a par. 2 of the Banking Ordinance). As far as market risks are concerned, each institution must provide for adequate internal limits. Other than the lending limits described beforehand, Swiss law imposes relatively few restrictions on lending activities of banks. There are no regulatory limits applied to lending to economic sectors or geographical areas, and there are no minimum lending requirements to certain economic sectors, social classes, or geographical areas. The basic rule governing lending activities is the standard of safe and sound banking, which includes a duty to properly establish and assess risk levels, including counterparty risk. In addition, the internal policies and procedures of banks must clearly define the type and geographical scope of the institution's business. Several banks have internal limits for industry sectors and in the case of the two largest banks, the SFBC receives quarterly, a breakdown of exposures by industry. The breakdown is based on the so-called NOGA-code (*nomenclature generale des activities*) and includes such industries as real estate, construction, oil and gas, telecoms, and automotive. Annually, all banks must report their 10 largest borrowers to the SFBC. Further, banks are under a duty to establish reporting lines, lending limits for each borrower and margin requirements. Finally, all loans must be properly documented in order to promote informed lending decisions and asset quality assessment by internal and external auditors.

	There are no fiscal arrangements for the lending business. However, a preferential regulatory arrangement exists for certain banks, where the upper limit of 25 percent of the eligible capital in the case of short-term claims (remaining duration of less than one year) on banks is reached very quickly as they must be weighted with a factor of 25 percent (Art. 12a par. 1 point 2.4 of the Banking Ordinance). In the area of risk diversification, the SFBC establishes a risk-weighting rate of 8 percent for short-term claims on large banks, cantonal banks with a cantonal guarantee and for claims on the RBA Central Bank held by banks of the RBA Group (group of more than 80 regional banks). In addition to that, a risk-weighting rate of 12 percent is established for short-term claims on foreign banks with a short-term rating "Prime 1" and a long-term rating "AA" or higher as well as a BIS capital of at least SwF 5 billion (per SFBC-Circular 00/1 of October 26, 2000 on less restricted risk diversification, Regulations for Claims with Residual Maturity of up to One Year on Certain Banks "short-term Interbank Claims "). All banks must comply with the lending limits described above. Moreover, since June 2000, banks must report the 10 largest claims on Swiss and foreign banks on a quarterly basis to the SNB where the data is collected, recorded and transmitted to the SFBC. The regular analysis of the data allows the SFBC to assess and to monitor a possible impact of financial difficulties of banks and systemic risks that might arise from them. The risk diversification rules are based on the general rules on capital requirements. For each position involving a counterparty, the risk weighting factor corresponding to this counterparty or to the collateral received pursuant to Art. 12a par. 1 of the Banking Ordinance should be applied. The risk weighting for certain counterparties (e.g., 25 percent for claims from other public sector entities in OECD countries) and for the collateral received (e.g., 50, 75, or 100 percent for claims directly or indirectly secured by mortgages on residential properties) allows banks a certain flexibility in their lending business within the current rules. In contrast to these general rules, for Lombard facilities which are secured by marketable assets which derive from a diversified portfolio and are traded on a recognized securities exchange or on a representative market (pursuant to Art. 12a par 1 point 4.3 of the Banking Ordinance), a risk weighting factor of 50 percent (instead of 75 percent) is applied. This kind of business has a very long tradition in Switzerland and the inherent credit risk is viewed as very low due to over-collateralization. In special cases the SFBC can allow an easing of the regulations of Art. 21– 21m of the Banking Ordinance, or it can order a tightening of them (Art. 22 of the Banking Ordinance). In practice, the SFBC follows a very restrictive policy and exceptions have only been granted in very limited special cases. The Banking Act, Banking Ordinance, and SFBC Guidelines impose limits on large exposures to a single borrower or "closely related group" of borrowers. These limits reflect actual risk exposure and include all claims and transactions, on-balance sheet as well as off-balance sheet. 10 percent or more of a bank's capital is defined as a large exposure and 25 percent of a bank's capital is the limit for an individual large exposure to a private sector nonbank borrower or a closely related group of borrowers. In special cases, deviations from these limits may be acceptable, if approved by the SFBC. During their annual bank audits, the external auditors verify that banks have management information systems which enable them to identify and monitor concentrations on a timely basis (including large individual exposures) within the portfolio on a solo as well as a consolidated basis. The external auditors and the SFBC regularly obtain information that details concentrations within a bank's credit portfolio and can determine if limits have been exceeded.
Assessment	Compliant.
Comments	
Principle 10.	**Connected Lending** In order to prevent abuses arising from connected lending, banking supervisors must have in place requirements that banks lend to related companies and individuals on an arm's-length basis, that such extensions of credit are effectively monitored, and that other appropriate steps are taken to control or mitigate the risks.

Description	The amount of loans to shareholders, officers and "other related parties" is detailed in Art. 4ter of the Banking Act, which states that such credits may be granted "only in conformance with generally accepted principles of the banking profession." However, such principles are not defined in the Banking Act, Banking Ordinance or any of the guidance issuances of the SFBC or the SBA. Art. 21 paragraph 3, of the Banking Ordinance addresses risk diversification and concentrations and covers such risk positions involving a member of the bank's governing bodies or a person who holds a qualified participation in the bank (i.e., a shareholder) or any person or body corporate closely related to them. Article 25c, paragraph 1 item 3.13 and the SFBC's Guidelines on Financial Statement Reporting Requirements (paragraphs 67, 92, 182-184) require insider lending be disclosed. However, neither the Banking Act nor the Banking Ordinance prescribe limits on such loans outside of the general caveat that such loans should conform to generally accepted principles of the banking profession. Although no specific guidance or circular has been issued on this particular subject, the SFBC states that there is strict supervision over such loans by the internal auditors, external bank auditors and the SFBC. Per the SFBC, "insider" loans should be granted on similar terms and at similar rates as loans to unaffiliated parties. On a quarterly basis, the banks have to prepare the “notification of risk concentration” report and submit it to the external bank auditor. Should the risk position involve a member of the bank’s governing bodies or a person who holds a qualified participation in the bank or any person or body corporate closely related to them, the risk concentration shall be designated accordingly in the list under the collective term “Transactions with Governing Bodies.” SFBC-Circ. 96/3 Appendix III requires banks detail their 10 largest borrowers annually; if an "insider" has a large exposure, that individual will be identified. Prudent practices would limit such credits to a specific amount that, as a percentage, would be covered separately by eligible equity. SFBC stated in their response to IMF's questionnaire that such loans shall not exceed 25 percent of eligible equity. This restriction is valid on an individual basis. On an aggregate basis, the amount of risk concentration for all such loans is the same as other concentrations and shall not exceed the percentage of 800 percent of the eligible equity. However, all loans to "insiders,” regardless of whether they meet the threshold of being a concentration, warrant review and scrutiny by the external auditors and the SFBC to ensure they are granted and monitored on an arm's-length basis without preferential terms granted. Pursuant to Art. 4ter of the Banking Act, commercially based lending and collection policies must be applied to loans to shareholders, officers and other related parties. The terms and conditions applied to loans to related parties must not be more favorable than credits extended to non-related borrowers under similar circumstances. During the annual external audit, related party loans are selected for review by the auditor to determine conformance with generally accepted principles of the banking profession. Any preferential treatment to such borrowers would be reported to the SFBC. Directors are expected to abstain from voting on their own or related party loans. The external auditor has discretion in making judgments about the existence of connections between a bank and other parties. The SFBC expectations are that generally accepted principles of the banking profession require that transactions with connected or related parties not pose undue risk to the bank and that such loans are addressed in a bank's loan policy with appropriate steps in place for underwriting, approval and monitoring repayment. The SFBC has set limits on loans to connected or related parties that are consistent with those associated with concentrations to any individual or related groups. Pursuant to circulars issued by the SFBC on the Long Form audit report the SFBC expects banks to have information systems to identify individual loans to connected and related parties as well as the total amount of such loans, and to monitor them through an independent credit administration process. The SFBC obtains and reviews information on aggregate lending to connected and related parties on a regular basis and external auditors check this area closely during their annual audit. Such loans are included in a bank's annual published report and the external auditor's Long Form report to the SFBC.
Assessment	Compliant.

Comments	
Principle 11.	**Country Risk** Banking supervisors must be satisfied that banks have adequate policies and procedures for identifying, monitoring, and controlling country risk and transfer risk in their international lending and investment activities, and for maintaining appropriate reserves against such risks.
Description	Art. 9 par. 2 of the Banking Ordinance requires banks to establish regulations or internal guidelines that address the main principles underlying the management of risks and the competencies and procedures for the approval of high-risk transactions. Specifically detailed in the Ordinance are market, credit, default, settlement, liquidity, and image risks as well as operational and legal risks, which must be identified, limited, and supervised. Although country risk and transfer risk are not specifically identified, they can be captured under any of the listed categories. The SBA issued qualitative guidelines for the Management of Country Risk dated September 4, 1997 and also has an issuance on Practices in Foreign Exchange Trading dated December 5, 1996 that are germane to transfer and country risks and the SFBC has concurred with the guidelines. Limits on all relevant risks a bank is exposed to are also a requirement stated in paragraph 1 of the Guidelines of the SBA for the Risk Management in Trading and in the Use of Financial Derivatives dated January 31, 1996. There are no explicit limits being imposed by the SFBC on open positions in individual foreign currencies but banks must have an adequate risk measurement system in place, which includes the setting of limits (paragraph 1 of the "Risk Management Guidelines for Trading and for the Use of Derivatives"). The size of these limits (e.g., EUR 200 million, US$500 million) and the limit type (e.g., intra-day or overnight, position limit or value-at-risk limit) are bank specific. Capital adequacy requirements are imposed on open foreign exchange positions. In 1983, the SFBC issued a circular requiring for the first time that internationally active banks allocate 20 percent of their general loan loss reserves to loans with a country risk. This percentage was retained until the end of 1988, when the rate was raised to 35 percent. Then beginning December 31, 1989, a distinction was made: the required general loan loss reserves for short-term trades with a maturity of at most one year was 10 percent, the one for other trades 50 percent. At the end of 1991 the required general loan loss reserves for the other loans was raised to 65 percent while requirements regarding general loan loss reserves were dropped. The regulation changed again in 1992 and every year the SFBC published a list of countries with the minimal rates for the general loan loss reserves (between 5 percent and 100 percent) for the individual countries and the types of business exempted from these specific provisions. The SBA issued Guidelines for the Management of Country Risk dated September 4, 1997, which impose on banks the obligation to introduce their own systems of identifying, controlling and measuring country risk. Under SFBC-Circular 92/4 (which was repealed as of January 1,1999), banks were to establish specific sovereign risk provisions with respect to all exposures in countries listed in an appendix to the circular. Provisioning rates were specified and subject to certain exemptions. The SFBC decided to repeal its circular because when considering the banks with the most significant country risks, the country risk reserves required, according to the circular, had decreased. The banks in this business asked the SFBC to exempt parts of their business from the general loan loss reserves. The guidelines of the SBA address more than provisions and include risk policy, recordation (identification and measurement), risk limitation and provisions, reporting and disclosure and audit. The SFBC felt these self-regulating guidelines, coupled with the banks' knowledge on specific countries, were more comprehensive than the SFBC circular. The banks' external auditors examine whether the guidelines have been adhered to, utilize rating agency information on particular sovereign risks, and record the audit results in the annual audit report and Long Form report that goes to bank and SFBC management. Banks are expected to review their provisioning for country risks at least semi-annually. The SFBC receives aggregate numbers on a country basis quarterly and further detailed information is incorporated in the annual external audit report. Under the Swiss tax code, bad debt reserves and country risk provisions are allowed as follows:

	– individual risks can be adjusted at the discretion of the bank, and these adjustments can be challenged at the discretion of the tax authorities. Provisions can be made before the debtor has been declared bankrupt. Write-offs of bad debts are made only when the debtor is adjudged bankrupt or it is highly unlikely that the debtor will ever be in a position to pay; – in addition, a general reserve can be made on the remaining outstanding receivables if the debtors are not banks in an OECD country. In general, 5 percent of the outstanding receivables from Swiss clients and up to 7 percent on the outstanding receivables from non-Swiss clients are allowed. All provisions must be reviewed annually and adopted. Failure to do so will lead to disallowance of excess bad debt reserves or of country risk provisions no longer being required. Only foreign banks and a few of the other Swiss banks, including the two large banks, are involved in cross-border or transfer risk activities. The SFBC does not receive monthly a Currency Report, broken down by country, from the applicable licensed institutions. However, the quarterly Large Exposures report also contains some country exposure information. The two largest Swiss banks report quarterly to the SFBC a breakdown of exposures for emerging market countries. Of the country/transfer risk exposure that exists, most of it is with/to large multinational corporate borrowers and OECD countries. Generally, the SFBC has not had much need to involve itself with cross-border and transfer risk given the limited number of banks involved. However, in those instances where a particular country is experiencing problems, the SFBC know which of its banks may have currency and large exposures in a particular region or country. The bank, its external auditor and the SFBC will review the data and the magnitude of the exposure and determine if any supervisory action is needed. In order to complete the SFBC's Large Exposures reports, banks must have policies, procedures and systems in place to identify, monitor and control country and transfer risks. As part of their on-site inspection, the external auditors review the banks' policies and procedures for adequacy. Lending policies should address the geographic spread of risk, including appropriate limits and then compare them to a bank's own internal country risk data. In addition, the Swiss Accounting Standards and the Tax Code address accounting for and disclosure of country and transfer risks. As previously noted, although not specifically required, banks are encouraged to apply the Swiss standards with respect to their financial statements, including adequate disclosure. Thus, banks involved in international lending must have the systems in place for identifying and monitoring country and transfer risks so that appropriate measures can be taken as/when needed. The SFBC, the Banking Act and Banking Ordinance all require credit institutions have in place appropriate policies relating to the management and control of the lending function. During the external auditor's on-site audit, auditors review an institution's loan administration, assess the internal controls, internal loan review function, problem loan policies and loans, review loan files against stated policies, review related management information systems and review management reports and any related actions taken. The SFBC no longer imposes blanket requirements regarding provisions on a country specific basis. The banks themselves determine the appropriate amount of provisioning, generally in accordance with standard accounting guidance. The appropriateness of a bank's provisions is reviewed annually by the external auditor in conjunction with the review of a bank's financial statements and also by the SFBC upon receipt of the audit report. Monthly prudential reports filed by the largest Swiss banks may provide details of provisions made and arrears statistics which allows the SFBC to monitor, off-site, any deterioration in banks' loan portfolios. The SFBC, in conjunction with information received from the banks and external auditors, determines that a bank's policies and procedures give due regard to the identification, monitoring and control of country risk and transfer risk with exposures identified and monitored on an individual country basis. Banks are required to monitor and evaluate developments in country and transfer risks, apply appropriate countermeasures and have information systems, risk management systems and internal control systems in place to comply with its policies. The SFBC permits the

	banks themselves to decide for each individual loan the appropriate provisioning in conjunction with the SBA's guidelines and in line with perceived and/or identified specific risks. The provisioning is judged by the external auditor and by the SBC for adequacy. The SFBC receives and reviews sufficient information annually via the external audit Long Form report on the country risk/transfer risk of individual banks.
Assessment	Compliant.
Comments	
Principle 12.	**Market Risks** Banking supervisors must be satisfied that banks have in place systems that accurately measure, monitor, and adequately control market risks; supervisors should have powers to impose specific limits and/or a specific capital charge on market risk exposure, if warranted.
Description	The SFBC-Circular 97/1 "Guidelines governing capital adequacy requirements to support market risks" focuses on capital adequacy but also covers market risk. Financial intermediaries applying the model-based approach have to observe detailed qualitative standards with respect to their market risk management process. In particular, they have to ensure that the risk aggregation model is closely integrated into the daily risk control. Its results must be an integral part of the planning, monitoring and management of the market risk profile of the bank. There must exist a clear and permanent relationship between the internal trading limits and the value-at-risk as it is used to determine capital requirements for market risks. The computation of required equity is made according to the rules set out in Art. 12a through 12o of the Banking Ordinance. The requirements to support market risks are further regulated through Guidelines issued in SFBC-Circular 99/1. The market risks may be computed using the standard approach described in the Banking Ordinance and Guidelines or, with the consent of the SFBC, using a model-based approach. The use of the model-based approach is conditional upon the bank fulfilling specific SFBC requirements. Simplified rules apply for computing capital charges on trading book positions if a bank's trading book at no time exceeds 6 percent of all on- and off-balance-sheet positions and the absolute level of SwF 30 million (so-called "*de minimis*" rule). EC Directive 93/6/EEC issued in March 1993 and amended in 1998, addresses the capital adequacy of investments firms and credit institutions and contains requirements for credit institutions in the area of market risk. Information, risk management and internal control systems must be in place for all areas, not just the market risk area. Although Switzerland is not a member of the EU and not required to implement EU Directives, generally the Swiss banks adopt the significant aspects of the directives into their own system since they are major competitors to EU banks. Swiss credit institutions are required to determine a trading book policy statement that sets out the basis on which positions are allocated between the trading and the banking books. The SFBC requires banks to assess associated market related risks (position, interest rate, settlement and counterparty, foreign exchange and large exposures) and identify, measure, monitor and control them. External auditors perform on-site audits annually using established industry procedures regarding Treasury/Market activities. Part of the procedures requires the auditors to review the banks' policies during on-site audits to ensure adequacy and suitability. The EC Directive was amended in 1998 to permit the use of models in identifying, measuring, monitoring and controlling market risks. In order to carry out its supervisory duties in the area of market risk, the SFBC has established a separate risk management unit that has specialists who review bank models and keep abreast of the products offered by those institutions identified from prudential reports as being market players. The unit goes on-site to those larger banks that have developed internal models for tracking, assessing and monitoring their market risks. The SFBC experts validate/evaluate the models in use. The SFBC plans to add five additional staff to the unit in the next few years in anticipation of finalization of the revised Basel Capital Accord that is currently under review. It is important for the banks and the SFBC to know what types of products are being traded and when they are due. This is an item for discussion when the SFBC meets quarterly with the largest Swiss

	banks. The SFBC does not approve models subject to any conditions. The staff discuss with the banks what a representative model would be and what it might factor into the assumptions. Although the SFBC does not conduct stress tests of the banks or system, individual banks have set up their own modeling scenarios to stress test shocks to the markets. Both large Swiss banks stated that the September 11 terrorist attacks in the United States tested their system but results at both banks were reportedly within the stress test parameters. The risk management staff reviews internal bank limits and their appropriateness in regard to the models. They review the bank's trading book policy statements and discuss the limits set for their various market risks and the appropriateness of the levels. These limits are subject to ongoing monitoring by the SFBC Risk Management unit. In addition to the on-site inspections, the SFBC collects details of the market risk incurred by the banks through the monthly Prudential Return, which the large banks with models provide. Information submitted includes interest rate, equity, foreign exchange, settlement/counterparty and large exposure risks arising due to a bank's trading activity. The SFBC does not prescribe specific limits on market risk exposures. For market risk, capital requirements are determined in line with the Basel Accord and Swiss standards at appropriate levels for each institution. Details of the supervisory process used by the SFBC's examiners during their on-site model validation inspections include review of a bank's treasury and market risk activities. The Risk Management staff is supported in their on-site inspections by external auditors and staff from the Large Bank unit. An important part of the on-site inspection, as well as the quarterly meetings with bank management, is to ensure that the Board and management understand the various products the institution offers and their associated risks. Information, risk management and internal control systems must be in place for all areas, not just the market risk area. Institutions are checked to see that they capture transactions on a timely basis and that positions are revalued using reliable market data. Inspection procedures specifically verifying confirmations, settlement, and reconciliation activities are important for overall operational validation. As part of the process, SFBC examiners determine that an institution has an appropriate number of traders for the type and volume of activity conducted. Most banks involved in market risk management are international institutions using some type of internal Value at Risk (VaR) model. The SFBC staff looks to an institution's internal and external audit processes for support in ensuring banks conduct periodic validation/testing of the systems used to measure market risk. SFBC's risk experts review approaches used for identifying and measuring risks with the banks in great detail. Banks conduct "extreme" scenario calculations and stress- and back-testing are done in instances where models are used for validation purposes. Contingency planning, in case systems fail, is a required part of a bank's risk management process. Both UBS and the Credit Suisse Group (Switzerland's two largest banks) have requested, and received, the SFBC's formal review and approval of their models (required under the Capital Adequacy Directive of the EU). As previously noted, Switzerland is implementing the models approach of the Directive even though it is not an EU member. Institutions with an approved model perform stress testing, scenario analysis and contingency planning, as appropriate, in addition to periodic evaluation and system testing. For the level of activity and the number of institutions involved in market activities, the Risk Management unit is adequately staffed. However, once the revision to the Basel Accord is finalized, if many more Swiss banks adopt the internal rating method for determining capital adequacy, the additional five planned staff positions plus possibly several more will need to be provided to ensure the requisite expertise to monitor market activity and review/assess banks' models. Resources could be stretched should multiple banks request approval of their models at the same time. The Banking Act and Banking Ordinance require all bank directors and senior management to have the appropriate competence and experience to enable them to fulfill their fiduciary duties. A bank must have in place comprehensive risk management systems commensurate with the scope, size,

	and complexity of all of its activities, incorporating continuous measuring and monitoring of risk, accurate, and reliable management information systems and timely management reports. During the SFBC's quarterly meetings and its on-site inspections, and in conjunction with the external auditors, the SFBC assesses the direct involvement of senior management in the market risk activities of the bank to ensure that management is kept informed of the activities and that senior management are exercising their duties responsibly. The role of the risk management function within the bank is carefully reviewed and its independence assessed. SFBC Large Bank and Market Risk units get monthly data from the largest banks, which facilitate timely review. Management reports are reviewed for completeness, accuracy, and timeliness. Management is questioned regarding their use of such reports and their overall knowledge of the products being offered by the bank. Stress testing assumptions are reviewed in conjunction with a bank's overall business plan/strategy, its operating environment and current market conditions. Stress testing scenarios and contingency planning are also frequent topics for discussion during the SFBC's quarterly meetings with bank management. The SFBC determines in conjunction with a bank's external auditors, that banks have suitable policies and procedures related to the identification, measuring, monitoring and controlling of market risk. These policies and procedures include setting appropriate limits for various market risks, including foreign exchange business. The SFBC has the power to impose a specific capital charge and/or specific limits on market risk exposures, including foreign exchange business and ascertains independently or in conjunction with external auditors that banks have information systems, risk management systems and internal control systems in place to comply with those policies. The SFBC and external auditors verify that any limits are adhered to and that there are systems and controls in place to ensure that all transactions are captured on a timely basis and positions are revalued frequently, using reliable and prudent market data. The SFBC has requested banks perform scenario analysis, stress testing and contingency planning, as appropriate, and periodically validate or test the systems used to measure market risk. The SFBC reviews the assumptions management has used in their stress testing scenarios, and the banks' contingency plans for dealing with such conditions. The SFBC reviews management's understanding of the bank's products and the quality of management information.
Assessment	Compliant.
Comments	
Principle 13.	**Other Risks** Banking supervisors must be satisfied that banks have in place a comprehensive risk management process (including appropriate board and senior management oversight) to identify, measure, monitor, and control all other material risks and, where appropriate, to hold capital against these risks.
Description	Within the scope of self-regulation, the Swiss Bankers' Association (SBA) has established guidelines for the management of country risks and guidelines concerning risk management in trading and the use of derivatives ("Risk Management Guidelines for Trading and for the Use of Derivatives" of January 1996 and "Guidelines for the Management of Country Risk" of November 1997). These two guidelines set out the professional rules concerning risk policy, risk identification, measurement and limitation, valuation, reporting and disclosure. The external auditors must describe and assess in their annual audit report the bank's risk management process, in particular the integrity of the input data, the measurement of risks, the monitoring of limits, the validation of models and procedures employed and their correct application and the reporting to management and the board. In addition, they must assess the independence and the integration of the risk management and risk control process into the bank's organization (SFBC-Circulars 96/3 "Audit Report," par. 16). The external auditors have to give their opinion whether a bank is in compliance with the applicable SFBC-Circulars and SBA-Guidelines. It is the responsibility of each bank's board to establish the entity's risk appetite and set appropriate

	limits commensurate with that appetite. The SFBC intercedes when a bank's appetite for risk results in its involvement in new activities. Since all activities must be detailed in a bank's bylaws, which are approved by the SFBC at the time of licensing, any new activities must be added to the bank's bylaws and the SFBC must approve all bylaw changes. This provides the SFBC with the opportunity to determine if a bank can handle the risks associated with a particular new activity. Where the SFBC has doubts, staff contacts the bank and discuss the proposed change. *Liquidity Risk.* The applicable liquidity requirements are set out in Art. 4 of the Banking Act and in Art. 15 to 20 of the Banking Ordinance. Liquidity management addresses a bank's ability to meet its actual and contingent obligations, various liquidity scenarios (day-to-day, liquidity crisis, market/worst case crisis), foreign and domestic currency positions, measurement systems and their underlying assumptions, contingency plans, funding sources and requirements, and overall liquidity management. Banks are required to maintain an emergency buffer to ensure that there are sufficient liquid funds in the banking system to protect the interests of creditors against the impact of any unexpected drain of money from the banking system. Liquidity management should include developing measurement techniques (such as GAP reports, VaR models, duration, or simulation models), procedures, and identifying an appropriate mix of assets and liabilities. Trading positions should be either closed or reduced to minimal levels at the end of each business day; tactical positions require daily management; and strategic positions, while generally stable, should be reviewed periodically to determine if change is needed. Following discussions with SFBC staff, GAP reports are not filed as part of the prudential reporting process and the current supervisory system for monitoring liquidity as part of the off-site supervision is in the process of review. The SFBC has mandated a working group to overhaul the current system and align the present liquidity requirements more closely with the Basel Committee's paper on "Sound Practices for Managing Liquidity in Banking Organizations." The working group hopes to develop a framework for liquidity analysis in the next year with implementation two to three years from now. Swiss banking law distinguishes between liquid (cash or first grade liquidity) and marketable assets (general or second grade liquidity). The cash liquidity serves to ensure that there are sufficient giro deposits with the SNB. The required liquidity is based on defined Swiss franc short-term liabilities. These liabilities include short-term deposits from banks and other creditors with a maturity not exceeding three months and 20 percent of savings, deposits and similar books or accounts, excluding pension fund liabilities. The base is computed as the average of outstanding balances at the end of the three months preceding the computation. The Federal Finance Department fixes an across-the-board cash-liquidity ratio for all banks based on recommendations of the SNB and the SFBC. Cash liquidity requirements may not exceed 4 percent of the above-mentioned average liabilities. Currently, the first grade liquidity ratio requirement is fixed at 2.5 percent (per the Ordinance of the Department of Finance of November 26, 1987). The required liquid assets must be held on average for the entire 30-day period from the 20th of the month following the calculation period to the 19th of the following month. The ratio is recalculated monthly based on the new average. Although one function of cash liquidity requirements is to allow banks to fulfill unexpected cash claims without recourse to credit facilities at other banks or the SNB, the main purpose of this across-the-board ratio is to enable the SNB to control monetary policy. For that reason, it was decided to transfer the cash or first grade liquidity regulation from the Banking Act and Banking Ordinance to the pending revised SNB Law. The total revision of the SNB Law is currently in consultation process. The across-the-board ratio will be set forth in Art. 17 (minimum reserve) of the revised SNB Law. The general or second grade liquidity is designed to ensure that a bank retains an emergency supply of liquidity to meet its own needs for a certain time. The short-term liabilities which form the basis for the computation include the excess of off-settable short-term liabilities (Art. 17a of the Banking Ordinance) over easily realizable off-settable assets (Art. 16a of the Banking Ordinance); 50 percent of short-term creditors and other accounts or books without withdrawal restrictions; and 15 percent of deposits in savings, deposits or similar books or accounts with withdrawal restrictions excluding amounts not available for distributions (e.g., pension fund liabilities).

	Based on this calculation, 33 percent of the total of these three components must be covered by liquid assets (Art. 15 of the Banking Ordinance) and easily realizable assets (Art. 16 of the Banking Ordinance). The levels of cash liquidity and general liquidity have to be maintained continuously. Banks must prepare monthly returns for cash liquidity and quarterly returns for the general liquidity. These returns are prepared on official forms and submitted to the SNB. If a bank does not meet the liquidity requirements the SNB must immediately give notice to the SFBC. Banks are also required to ensure that adequate levels of liquidity are maintained on a group-wide basis. *Large Exposure Risk.* Banks are required to notify their external bank auditors whenever their sight and other liabilities due within one month to a single customer or bank exceed 10 percent of their total (not netted) sight and other liabilities due within one month. The liabilities to a single customer include those to parties related to the customer when there are majority interlocking shareholdings. The auditors must include this information in their annual audit report. They must recommend corrective action if the funding appears to be inappropriately concentrated. One of the criteria for holding a banking license is the establishment of an adequate organization corresponding to the business activities (Art. 3 of the Banking Act). Art. 9 par. 2 of the Banking Ordinance states that financial intermediaries have to document the main principles for the management of risk and the competencies and procedures for the approval of taking risks in internal guidelines. They must in particular identify, limit, and supervise market, credit, default, settlement, liquidity risks as well as reputational, operational and legal risks. *Market Risk.* See CP 12 above. *Interest-rate risk.* SFBC-Circular 99/1 dated March 25, 1999 on "Measurement, Management and Monitoring of Interest-Rate Risks" sets out the minimum standards to be applied in the measurement, management and monitoring of interest-rate risks. The external auditors ensure that the banks' standards cover foreign and domestic currency positions and include reviewing measurement techniques used to assess interest rate risk and the underlying assumptions, reviewing MIS for timeliness and accuracy, and reviewing simulations of interest rate scenarios (increasing and decreasing). In addition, banks have to report to the SFBC their risk exposure on a cash flow basis. Based on this information the SFBC will be able to identify outlier banks, that is, banks with a significant risk exposure. The supervisory review process reveals whether such risk exposure is in line with the bank's implemented risk management policies and procedures. If the identified risk exposure is deemed to be too high, an additional capital charge will be levied on the bank by the SFBC. *Foreign Exchange Risk.* Sound banking practices require banks set overnight open position limits and intra-day limits. The largest banks conduct their business in this way and guidance is available in SFBC-Circular 97/1 dated October 22, 1997, as amended October 1, 1999. External auditors verify on behalf of the SFBC that limits for more volatile and less liquid currencies are lower than those for stable and liquid currencies, and that long positions in currencies susceptible to devaluation or that lack ready availability are strictly limited in conjunction with safe and sound practices. *Operational Risk.* Such risk crosses all business lines and can be more significant in the asset management investment lines than in the more traditional banking activities of lending. The SFBC requires every banking entity licensed to conduct business have an internal auditor and/or internal audit function to monitor the entire institution and in the process of such monitoring, reduce overall operational risk. The SFBC and sound banking practice supports a Board audit committee chaired by a non-management person with a direct reporting line for the internal auditor. If there is no Board committee in the licensed entity (which happens in branches and small subsidiaries of international institutions), then the auditor must have a direct reporting line to the entity's Chairman of the Board. As noted above, the SFBC is in the process of reviewing and possibly replacing the current liquidity ratio concept with a new approach. Incorporating stock and maturity mismatch (or gap-based) approach and including contingencies and off-balance sheet items should result in a more up-to-date measurement process. External audit procedures require auditors determine the appropriateness,

	adequacy and suitability of the processes in place during on-site inspections, including whether limits and procedures are operating effectively and appropriate responsibility is assigned to the relevant business units and personnel based on their operations. The SFBC's supervisory process includes regular collection and analysis of data; regular review meetings with senior bank management and external auditors; review of audited accounts and Long Form audit reports; approval of proposals for new business activities; and ad hoc meetings, correspondence, and phone calls with the banks as the need arises. On a monthly basis the SFBC receives prudential data, which permits it to verify a credit institution's compliance with the liquidity requirements. In addition, the SFBC is immediately notified should a bank have a shortfall of its capital requirements. SFBC's examiners review banks' internal audit reports which can indicate areas of potential concern and meet with banks' external auditors as deemed necessary to supplement qualitative assessment. During the external auditor's on-site inspections, the auditors verify the accuracy of the data submitted and determine whether risk management processes are operating effectively. The frequency of inspections depends on an institution's structure, quality of ownership, size, financial condition, risk profile, profitability (current and trend), activities, and the SFBC's perception of management. Institutions where the SFBC is the "home country" supervisor (Swiss owned banks) are required to receive an annual on-site audit performed by an audit firm approved/licensed by the SFBC. See CP 6 for details regarding capital adequacy requirements for banks based on a risk assessment. Swiss banks adhere to the current Basel Accord with more stringent standards imposed by the SFBC. Banks are encouraged to follow or be standard setters for best practices on corporate governance issues, including the disclosure of a statement on risk management policies and procedures in their published financial statements. Financial reporting standards, which apply to all banks and financial institutions, require that an explanation of the role financial instruments play in creating or changing the risks that the entity faces in its activities be disclosed in their public accounts. In addition, the institutions are required to explain the directors' approach to managing each of these risks, including a description of the objectives, policies and strategies for holding and issuing financial instruments. The SFBC requires individual banks to have in place appropriate board and senior management oversight of its comprehensive risk management processes that identifies, measures, monitors and controls material risks and are periodically adjusted in light of the changing risk profile of the bank and external market developments. The SFBC in conjunction with the banks' external auditors determines that the risk management process addresses liquidity risk, interest rate risk, and operational risk as well as all other risks, including credit and market risk. The external auditors address liquidity risk, interest rate risk, foreign exchange risk, and operational risk in their audit standards and on-site procedures. The SFBC sets liquidity guidelines for banks, and ensures external auditors determine that the risk management processes, capital requirements, liquidity guidelines, and qualitative standards are being adhered to in practice. The SFBC has the authority to require a bank to hold capital against risks in addition to credit and market risk.
Assessment	Compliant.
Comments	GAP reports are not filed as part of the prudential reporting process and the current supervisory system for monitoring liquidity as part of the off-site supervision is in the process of review. The SFBC should continue investigating ways to improve its current liquidity monitoring to align it more closely with the Basel Committee's paper on managing liquidity in banking organizations.
Principle 14.	**Internal Control and Audit** Banking supervisors must determine that banks have in place internal controls that are adequate for the nature and scale of their business. These should include clear arrangements for delegating authority and responsibility; separation of the functions that involve committing the bank, paying away its funds, and accounting for its assets and liabilities; reconciliation of these processes;

	safeguarding its assets; and appropriate independent internal or external audit and compliance functions to test adherence to these controls, as well as applicable laws and regulations.
Description	According to Art. 9 par. 4 of the Banking Ordinance banks must provide for an effective system of internal control. This includes an effective internal segregation of functions between trading, asset management and back office. The SFBC may grant an exemption in certain justified individual cases or require, in addition, the segregation of other functions (Art. 9 par. 1 of the Banking Ordinance). The management of the bank must assemble all documents concerning transactions with risks, which are necessary for taking decisions and monitoring such risks. These documents must also enable the auditors to form a reliable opinion on the business transactions (Art. 9 par. 3 of the Banking Ordinance). The SBA Guidelines concerning the concept and organization of internal audit in banks, dated from 1978, as amended in 1987, is currently under revision. The SFBC-Circular 95/1 dated December 14, 1995, provides guidance on Internal Audit and in their annual audit, external auditors are required by SFBC-Circular 96/3 dated October 21, 1996, to assess the appropriateness of internal control and the internal audit function. The EU's Second Banking Directive (89/646/EEC) issued in 1992 and adapted by the SFBC in several respects, also sets out requirements relating to internal controls. Swiss banks are required to have comprehensive risk management systems commensurate with the scope, size and complexity of all the bank's activities, and to continuously measure, monitor and control risk. Such systems must be accurate and reliable, and include timely management reporting and sound internal controls. Internal control systems and reporting arrangements should provide for the effective, prudent and efficient administration of (an institution's) assets and liabilities. It is the Board's and Management's responsibility to ensure that the business of the credit institution is being managed, conducted and controlled in a prudent manner. These are sound Corporate Governance requirements for Board and senior management involvement in the operations of credit institutions. (See CP 13 for discussion of Operational Risk management, which crosses over into all business units.) An internal audit function is required per the SFBC and good corporate governance standards. A good internal audit program is designed to include procedures to counter fraud. Management's strategic plans are reviewed to assess plans for (and the impact of) major system changes and how the bank is being positioned to deal with changes in their business environment. Management resumption plans were developed and reviewed in connection with planning for Y2K; the SFBC and external auditors should determine that such plans are kept up-to-date going forward, particularly in light of the September 11 terrorist attacks in the United States. According to Art. 9 par. 4 of the Banking Ordinance, a bank must appoint internal auditors independent from the management. The SFBC may, in certain justified individual cases, exempt a bank from the obligation of appointing internal auditors. The reports of the internal auditor must be submitted to the external auditor and in the case of the largest banks, the SFBC's large bank unit also reviews internal audit reports. The internal auditor has to communicate to the external auditors all information needed by them to fulfill their duties. The internal and the external auditors have to coordinate their activities to avoid duplication of auditing efforts as far as possible (per Art. 19 par. 3 of the Banking Act and Art. 40a of the Banking Ordinance). SFBC-Circular 95/1 of December 14, 1995 on Internal Audit further requires that the internal auditor be selected by the board of directors, report directly to it and execute the supervisory tasks, which have been transferred to it. In this connection, it is important to note that no member of the board of directors shall belong to the bank’s management (per Art. 8 par. 2 of the Banking Ordinance). The Internal Audit circular details the rules for the organization, the personnel requirements and the field of activity of the internal audit function. The circular also states that the internal audit function can be transferred to the internal audit of the parent company or another group company or an auditing firm recognized by the SFBC but must be independent of the external auditors of the enterprise. Independent third parties who can demonstrate a thorough knowledge of banking and bank auditing are permitted to serve as internal auditors. The external auditors have to comment in the bank's annual audit report in connection with the assessment of the compliance with the licensing requirements on the appropriateness of the internal

	audit (SFBC-Circular 96/3 Audit Report, par. 14). The assessment of the internal audit area includes staff qualifications and numbers, independence, audit work plan, audit procedures, work papers, and reports. Internal manuals on credit, foreign exchange and other market activities are required as part of sound corporate governance and should correspond to the business activities of a bank. Such is necessary to obtain and retain a banking license. The external auditor is responsible for assessing global controls in those banks with foreign operations. Deficiencies in foreign operations should be identified first by internal auditors. External auditors, in addition to assessing the adequacy of controls and internal audit, must also assess the fitness and propriety of the board and management in carrying out their fiduciary responsibilities. Both internal and external auditors review systems as well as controls. The lead external auditor is required to change every seven years to avoid the auditors losing their objectivity in regard of any one bank. Corporate or banking laws identify the responsibilities of the board of directors with respect to corporate governance principles to ensure that there is effective control over every aspect of risk management. The SFBC requires that banks have in place internal controls that are adequate for the nature and scale of their business. To achieve a strong control environment, the SFBC requires that the board of directors and senior management of a bank understand the underlying risks in their business and are both committed to, and legally responsible for, the control environment. The SFBC has the legal authority to require changes in the composition of the board and management as well as in the external audit firm. The SFBC requires that banks have an appropriate audit function charged with (a) ensuring that policies and procedures are complied with and (b) reviewing whether the existing policies, practices and controls remain sufficient and appropriate for the bank's business.
Assessment	Compliant.
Comments	
Principle 15.	**Money Laundering** Banking supervisors must determine that banks have adequate policies, practices, and procedures in place, including strict “know-your-customer” rules, that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements.
Description	Money laundering was made a crime by Art. 305bis of the Swiss Penal Code (Criminal Code) and all banks and other financial intermediaries are now required to comply with certain due diligence obligations with the passage of the Money Laundering Act (MLL) on October 10, 1997, effective April 1, 1998. Art. 305ter of the Criminal Code impose a general obligation to ascertain the identity of customers and beneficial owners of accounts. Violation is punishable with imprisonment of up to one year. In the financial sector, the SFBC issued its first circular on the subject in 1991 to all licensed banks and auditing firms containing guidelines for preventing and combating money laundering. This circular is presently being revised and the current version is SFBC Circular 98/1 dated March 26, 1998. The SFBC's circular complements the Swiss Banks' Code of Conduct and the MLL in that it sets out certain requirements regarding internal operating procedures, and refines the due diligence requirement with respect to cases where a heightened degree of diligence is necessary. Switzerland has implemented legislation for identifying, tracing, freezing, seizing and forfeiting narcotics-related assets. The Swiss banks self-regulation has been an essential part of the fight against money laundering. The Due Diligence Agreement has been in place since 1977, prior to the 1998 Anti-Money Laundering legislation and is deeply enshrined in the Swiss banking system. The Due Diligence Agreement is revised every five years and lists the following duties which banks must comply: – duty to ascertain the identity of customers – duty to ascertain the beneficial owner of assets

	– duty to verify specific aspects – duty to retain documentary records – duty to take appropriate organizational measures. In 2000, the two large Swiss banks joined with nine other internationally active banks to form the "Wolfsberg Anti-Money Laundering Principles," These principles are based on the Due Diligence Agreement but do not set out any sanctions or penalties. Adoption of and compliance with the principles are voluntary by the banks but have been agreed to by UBS and the Credit Suisse Group. Switzerland is a member of the Financial Action Task Force (FATF) on money laundering and was accepted into the Egmont Group of financial intelligence units in 1998. Switzerland has ratified the Council of Europe Convention on Laundering, Search, Seizure, and Confiscation of the Proceeds from Crime of 1990. In December 2000, Switzerland signed the United Nations Convention Against Transnational Organized Crime. Switzerland also has a Mutual Legal Assistance Treaty in place with the United States to exchange records and provide information in connection with narcotics investigations and proceedings. The Swiss signed a declaration of intent with the Belgian reporting office laying out details of cooperation in 1999 and are also negotiating similar arrangements with France, Finland and the Czech Republic. On December 22, 1999, the Efficiency Bill was passed by Parliament. The purpose of this bill is to make the prosecution of organized crime, money laundering, corruption and other white-collar crime more effective, by increasing personnel and financing of the criminal police of the Federal Office of Police (FOP). The new law gives the FOP and Attorney General's Office the authority to handle cases with international scope, involve several cantons, and deal with money laundering, organized crime, corruption, and white-collar crime more effectively. The law modifies Art. 340bis of the Criminal Code and takes effect on January 1, 2002. The SFBC ensures that banks have adequate policies, practices and internal operating procedures in place that promote high ethical and professional standards and prevent the banks from being used, intentionally or unintentionally, by criminal elements. The prevention and combating of money laundering is to be given due weight in the training of personnel, in particular of the employees having customer contacts. Beginning at the licensing phase, the SFBC relies on the external bank audit process to confirm that banks take the appropriate steps to prevent and detect criminal activity or fraud and report any suspicious activities to the appropriate authorities. Such steps must continue to be in place once a bank commences business and are reconfirmed annually by the external auditor. Banks must provide for internal operating procedures and control mechanisms necessary for the prevention and combating of money laundering. They must ensure adequate training of their personnel, in particular of employees having contact with customers. Each bank has to designate one or more persons or a specialized body (e.g., legal or compliance department) which advises the management and all employees in developing and implementing the internal operating procedures, in training personnel, in spotting cases of suspicious customers and transactions, and in all other questions related to money laundering. Internal auditors have to review the measures taken. Procedures are checked annually by the external auditors and any deficiencies require corrective action. SFBC-licensed external auditors determine that banks have complied with the law, SFBC guidance and the Due Diligence Agreement. Such annual audit attestations are part of the Swiss anti-money laundering program. As noted above, clear rules and guidelines are in place regarding what records must be kept on customer identification and individual transactions. Documentation must be retained for a minimum of 10 years after the account relationship is closed. The banks must investigate the purpose and economic background of transactions or business relationships appearing unusual unless their legality is clear (Art. 6 lit. a MLL). The banks must conduct further investigations if a customer or third party, at the time of opening an account or business relationship with the bank, deposits, for the credit of an account or security deposit, bank notes, securities or precious metals in a value equal to more than SwF 100,000. If a customer or third party, during the period of the business relationship, deposits or withdraws bank notes,

	securities or precious metals for the credit or debit of his deposit account, and the amount of the individual transactions or the number of transactions appear unusually high in relation to the known business activity and the known financial circumstances of the customer, the same procedure applies. The banks must set forth the framework for these investigations in their internal operating procedures for action. If the bank becomes aware of indications that certain funds originate from a crime, or that a criminal organization has the power of attorney with respect to these funds, special investigations are required to assess satisfactorily the background of the transactions. The banks must require for this purpose either a written declaration of the contracting party or prepare a memorandum for the record in which they must set forth the result of the investigations. Depending on the circumstances of each case, in principle, particular information is required on: – the purpose and nature of a particular transaction; – the financial circumstances of the contracting partner or the beneficial owner; – the professional or business activity of the contracting partner or the beneficial owner; – the origin of the funds deposited or invested. The SFBC as the supervisory authority for banks, securities dealers, stock exchanges and investment funds is also responsible for the supervision of the anti money laundering implementation with regard to these institutions. The approved external auditing firms are required to verify the implementation and application of the anti-money laundering rule in the context of their regular auditing activities. Violations must be immediately reported to the SFBC. Art. 8 MLL requires banks to take all measures necessary to prevent money laundering. They must make sure that their personnel are adequately trained and instructed and that regular internal controls are developed and followed. If a bank knows or has a justified suspicion that funds are connected with money laundering, it must notify the Money Laundering Reporting Office (MROS) immediately. For the year 2000, 311 reports were filed in total of which 234 (75 percent) were filed by banks. The SFBC should also be notified when serious issues are evident or in the case of noncompliance. The obligation to notify is also triggered if a customer refuses to cooperate in investigations. If a bank continues with a business relationship despite having doubts about it but without a well-founded suspicion and without informing the relevant authorities, it must monitor the business relationship. If a bank breaks off the relationship without informing the relevant authorities, it must ensure that the assets are withdrawn in a form that allows the prosecution authorities to follow the “paper trail” if necessary. The bank must not pay out large sums of money in cash or physically issue securities or precious metals. These obligations also apply if the bank suspects corruption or misuse of public funds. The bank must not break off the business relationship or allow the withdrawal of large sums if there are concrete indications that the authorities are about to undertake seizure steps. Once notification has been made, banks must block the funds without delay and maintain the freeze until they receive a ruling from the criminal authorities but for no longer than five working days. Banks must neither inform the customer nor third parties about the notification and the freezing of the funds if not permitted by the criminal authorities. The banks must prepare files on their customers to document relationships, transactions and investigations sufficiently to permit a third-party professional, such as the external auditor, to reach a reliable opinion about the transactions and the compliance with the law and the implementing SFBC Circulars. The identification document as well as the documents concerning the transactions undertaken have to be retained for at least ten years after the cessation of the relationship or the transaction (Art. 7 MLL). Banks must designate one or more persons or a specialized body who can ensure compliance with internal procedures and policies and advise the management and train all employees in cases of suspicious transactions or customers. Internal auditors must review the measures taken by the bank to prevent and combat money laundering. The SFBC Guidelines apply to the consolidated bank and provide that banks must not misuse their

	foreign branches and financial companies to circumvent the money laundering guidelines. They must ensure that banking group companies and establishments in countries that are not members of the FATF, follow the FATF recommendations applicable. The SFBC may prohibit banks from establishing affiliates in countries where the regulatory environment, in particular the anti-money laundering regulation, is deemed inadequate. Swiss banks' foreign offices must abide by the Swiss standards of due diligence as set forth in the SFBC Circular and the Swiss Banks' Code of Conduct and external audits of offices in foreign jurisdictions are done by Swiss auditors familiar with the Swiss standards. The SFBC may also order a "special audit" to verify compliance with the anti-money laundering provision. The SFBC mandated a special audit after serious omissions and organizational shortcomings were disclosed in a number of banks in Switzerland following a high profile case. The audit covered several establishments of the banks both within and outside of Switzerland. In addition to the "special audit," the SFBC may, within the context of regular consolidated supervision activities, require examination with a special focus on anti-money laundering procedures. In January 2001, the SFBC asked Swiss banks with significant activities outside of Switzerland to mandate that their auditing firms conduct in-depth examinations to verify the adequacy of their internal procedures, systems and controls governing anti-money laundering. These in-depth examinations place a particular focus on the adequacy and effectiveness of customer identification procedures, the functioning of internal control mechanisms and the communication and cooperation between internal audit and external audits. In addition, the auditors are required to report immediately to the SFBC any indications that the foreign establishments are used to circumvent Swiss legal requirements and professional rules. In the event of non-compliance, the SFBC shall impose administrative sanctions and may refer the violation to the criminal authorities. The SFBC has a range of sanctions available for banks in violation of the money laundering rules. Sanctions range from a reprimand to a special audit and/or dismissal of bank officials to the revocation of a bank's license if licensing criteria are no longer met or the bank is in serious breach of its legal obligations. Besides administrative measures, the SFBC may, in case of violation of the Banking Act, the MLL or the Criminal Code, bring criminal charges. Compliance with the Code of Conduct is enforced by an independent Supervisory Board set up by the Swiss Banker's Association (SBA). This Board may impose fines up to SwF 10 million. According to Art. 9 MLL, a bank who knows or has a justified suspicion that the funds in a business transaction are related to a criminal act as defined in Art. 305bis of the Criminal Code, must notify without delay the MROS. Banks cannot invoke banking secrecy provisions with regard to criminal or administrative authorities conducting investigations. They must provide all information requested by these authorities and allow access to all their files. Banking secrecy or confidentiality provisions therefore cannot hamper anti-money laundering investigations. The Criminal Code allows bank employees to report suspicious transactions without fear of violating the bank secrecy regulations. The SFBC and the SBA are in the process of updating the Due Diligence guidelines to clarify foreign corruption (currently addressed under the old law) and the duty for top bank management to know the big/high profile customers and to frequently check such accounts. These efforts are not limited to foreign corruption but also include a working group to revise the current SFBC money laundering circular. The working group consists of representatives of the Money Laundering Control Authority, the Money Laundering Reporting Office, and cantonal enforcement agencies. The objective is to also formulate recommendations for a review of the SBA's Code of Conduct on Customer Due Diligence. The revised SFBC guidelines will address: – Formulation of a more differentiated approach to customer identification; – Rules for non-face-to-face customer relationships, in particular internet-only banks; – Rules regarding identification of customers by third parties and independent asset managers; – More detailed rules on the verification of the beneficial owner; – Use of client profiles;

	– Heightened due diligence requirements in special cases, for example, Politically Exposed Persons (PEPs); – Adaptation of the existing rules to the criminal code provisions regarding foreign corruption and criminal liability of corporations. On March 29, 2001, the SFBC addressed a letter to all banks stating the minimum standards for account openings and the monitoring of accounts with "Internet only" banks. The letter currently imposes the same due diligence standards on such "virtual" bank account openings as on "brick and mortar" banks. These minimum standards will be subject to review and incorporated into the revised SFBC Anti-Money Laundering Circular. The minimum standards of March 29, 2001, will remain in force until their inclusion into and the issuance of the revised SFBC Anti-Money Laundering Circular. The SFBC requires, and periodically verifies via the dualistic supervisory process with external auditors, that banks have in place adequate policies, practices and procedures that promote high ethical and professional standards and prevent the bank from being used, intentionally or unintentionally, by criminal elements. Such policies, practices and procedures include the prevention and detection of criminal activity or fraud, and reporting of such suspected activities to the appropriate authorities. The SFBC requires banks to appoint a senior officer or committee with explicit responsibility for ensuring that bank policies and procedures are, at a minimum, in accordance with local statutory and regulatory anti-money laundering requirements. Laws, ordinances and guidelines and/or banks' policies protect staff who report suspicious transactions in good faith. The SFBC has adequate regulatory enforcement powers but has no criminal enforcement powers. It can impose administrative sanctions and, if criminal violations are found, the SFBC must inform the competent criminal enforcement authorities to take action against a bank that does not comply with its anti-money laundering obligations. The SFBC is able, directly or indirectly, to share with domestic and foreign financial sector supervisory authorities information related to suspected or actual criminal activities. However, one area where the SFBC would appreciate, and should have, clear legal enforcement authority is in their right to publish the identities of banks and individuals involved in money laundering activities and to impose monetary penalties for noncompliance with the MLL. The SFBC currently has established the practice of naming offenders in money laundering cases and providing a clear legal basis for the practice in law is desirable. Any new legal enforcement authority should not limit the SFBC to violations of the Money Laundering Act but rather apply more generally to all kinds of violations of a certain degree of seriousness, including violations of prudential rules and regulations in addition to violations of due-diligence and the anti-money laundering rules. The SFBC via the external audit process determines that banks have a policy statement on ethics and professional behavior that is clearly communicated to all staff. The Swiss laws and/or regulations embody international sound practices, such as compliance with the relevant forty Financial Action Task Force Recommendations issued in 1990 (revised 1996) and a 1998 FATF evaluation concluded that Switzerland has a comprehensive and solid legislative scheme in place to combat money laundering. Switzerland has been vigilant in developing anti-money laundering policies, and allocating resources to prevent money laundering. Information related to suspected or actual criminal activities is shared by way of various international agreements.
Assessment	Compliant.
Comments	Although the banking sector is compliant and diligent in complying with Switzerland's Money Laundering Act, the mission was not in a position to assess the effectiveness of measures introduced outside the financial sector.
Principle 16.	**On-Site and Off-Site Supervision** An effective banking supervisory system should consist of some form of both on-site and off-site supervision.

Description	Bank supervision for the vast majority of Swiss banks can be viewed as a three-pillar approach: The indirect supervision of the SFBC, the direct supervision of the external auditor, and the ongoing on-site supervision of the internal auditor. In addition, a fourth pillar, the Swiss Bankers Association (SBA) acts as a self-regulatory body and adds to the Swiss system of supervisory checks and balances. The internal audit function of the banks has been previously discussed in the assessment of CP 14. Also see CP 19. The Swiss system, also referred to as a "dualistic system," relies traditionally on the banks' external auditors, which perform an official supervisory function with respect to the financial intermediaries subject to SFBC supervision. The external auditors are part of the supervisory system. They are licensed and supervised by the SFBC. The external auditors carry out official duties and can be subject to sanctions imposed by the SFBC, that is, withdrawal of their license and replacement of the external auditor. In case of an external auditor violating the banking law, the SFBC must inform the Swiss Federal Department of Finance, which is the competent authority for the imposition of fines. The appointment of the external auditor by the bank is effected under private law, however the scope of the audit is laid down under public law in the Banking Act, the Banking Ordinance and the guidelines of the SFBC. The SBA is a very influential body in Swiss banking. It consults and cooperates with the SFBC on the development of new banking legislative proposals as well as draft ordinances and SFBC guidance circulars. The SBA also has initiated and established rules and conventions in consultation with the SFBC which SBA members are obliged to follow. Frequently such self-regulating guidelines are endorsed by the SFBC and then become of the same legal weight as SFBC issued guidelines and become applicable to all Swiss banks. Recent examples include legislation against insider trading and money laundering. The SBA is also very active in maintaining a code of ethics for the Swiss banking community. The Agreement on Swiss Banks Code of Conduct with Regard to the Exercise of Due Diligence of Banks is an example of such industry setting standards and procedures. External auditors are obligated to verify compliance with the professional rules of the SBA in the annual audits of the banks. The SFBC has a supervision staff of about 100 of which approximately 13 are in the large bank program. As part of its ongoing supervision of credit institutions, the SFBC performs primarily off-site assessments using a combination of quantitative and qualitative supervisory techniques, including external auditors. On-site supervision by the SFBC is limited to the market risk unit and the large bank unit. The principle quantitative measures require key ratios relating to minimum capital and liquidity levels, large exposures, lending to connected parties, and to individual economic sectors, concentration of deposits and acquisitions by banks in other entities and by other entities in banks. The supervisory process is interactive in nature and often entails dialogue between the SFBC, the auditors and the banks. The process draws its strengths from the principle of cooperation by the management of the institutions with the SFBC. The SFBC's supervision incorporates: regular collection and analysis of data; regular review meetings with bank management and external auditors; dealing with new issues as they arise; and the on-site inspections provided by the external auditors. However, data of detailed asset quality information (e.g., classified assets, past due loans, renegotiated credits and impaired loans) is limited and consideration should be given obtaining this type of information from all banks on a quarterly basis. Once obtained such information along with balance sheet growth and the profit and loss statement could form the basis for development of an early warning system. Regarding this disclosure see also CP 21. Of particular note is the shift in the last few years toward more direct supervision by the SFBC for its largest two banks. The SFBC created the large bank unit in 1998 to provide more direct supervision of these entities due to their significance to the Swiss market and economy and their extensive global operations. The large bank unit changed considerably the Swiss supervisory strategy for these banks, which had been based primarily on reporting by the external auditors. The new supervisory approach still comprises the traditional instruments of the indirect supervision (Long Form audit report in accordance with the Banking Act, meetings with external and internal audit), but also applies the customary tools associated with direct supervision, such as regular

	quarterly meetings with the bank management, supervisory visits, on-site reviews, regulatory attendance, standardized additional information requirements, and regular meetings with host regulators. The SFBC also has assumed a direct role in the area of evaluating and validating VaR models developed by the large banks and other major market banks for determining capital requirements for market risks in their trading books. Both the large bank and risk management units of the SFBC have been well received and accepted by the institutions. The main tool used by the SFBC for the supervision of all Swiss banks is the annual Long Form report (audit and inspection report) prepared by the external auditors on each bank in the system. The SFBC receives a copy of the report, reviews it and then meets with the external auditors to discuss any issues and the scope of activities for the applicable banks for the next supervisory cycle. If problems are noted, the SFBC may also schedule a meeting with bank management to discuss the results of the report. Other than the two largest banks, the SFBC meets with bank management in the remaining institutions once every three years unless problems surface requiring more frequent meetings. Art. 47 of the Banking Ordinance states that the audit report must be remitted within one year after the date of the financial statements or a shorter time period stipulated by the SFBC. The SFBC states that the reports are generally received within four months. The four-month period appears reasonable given that the report is one of the SFBC's most important off-site supervisory tools. If a Swiss bank is a part of a banking group which is supervised on a consolidated basis by the SFBC, the annual Long Form report will contain the auditor's opinion on a consolidated basis on the bank's organization, management, capital adequacy, large exposures, liquidity, internal audit, internal controls, and financial and risk profiles. External auditors also include in the Long Form report a detailed list of all engagements entrusted to them by the bank in order to address any matters that could impair their independence. The annual Long Form reports are reviewed by the SFBC and discussed with the auditor regarding content and quality. In addition, annual meetings between the SFBC and each licensed audit firm are held, where general issues as well as all audited banks are discussed. The audit firms have to hand in to the SFBC a report on their activities covering organizational, management, human resources, independence and audit procedure issues on an annual basis. If the SFCB has reasonable doubts on the performance of the audit in an individual case, it carries out a procedure to clarify if the audit is performed in compliance with SFBC guidelines. The SFBC may request another properly qualified auditor to review the institution and if the doubts are proven the SFCB can impose sanctions on the initial audit firm and lead auditor such as withdrawal of the license, replacement of the external auditor and fines. The annual Long Form reports are analyzed by the Banks / Securities Firms Supervision Department, which employs 23 people. In addition, the department processes notifications and inquiries of the supervised institutions and deals with questions of interpretation and of principle that are of importance for the supervision of licensed institutions. The department is responsible for the continuous supervision of all banks and securities firms that do not belong to one of the two large Swiss banking groups. In the last few years, supervision has become more risk-focused with the SFBC creating the large bank unit. In the case of the large banking groups, the supervision and analysis of the annual Long Form reports is carried out by the Large Banking Groups department. Members of this department also carry out supervisory visits or attend on-site inspections conducted by the banks' external auditors (“regulatory attendance”). SFBC management and staff appear well apprised of the condition of their portfolio of banks, and the conditions and composition of the business activities do not seem to change on a monthly or even quarterly basis. Usually prudential reports are used as a supplement to the annual Long Form report. The large bank group prepares a formal financial and risk profile, which is submitted to the SFBC management on a quarterly basis. The profile includes: – information from the regular quarterly meetings with Executive Boards and Group Executive Boards; – information from the regular quarterly meetings with the external auditors;

	– information from the regular annual activity reports and audit plans of internal audit; – the SFBC's assessment of the consolidated risk reports prepared by the two financial conglomerates; and – the SFBC's assessment of quarterly global credit and market risk reports provided by the two investment banking business units UBS Warburg and CSFB. Consideration should be given to formalizing the process of regular meetings, on-site exams, etc. for the large banks by adding to the annual risk profile of each credit institution. The profile should utilize off-site data as well as information obtained from trilateral meetings with foreign supervisors, insurance supervisors, management, and external auditors. When developing an institution's risk profile, the SFBC should specifically focus on any gaps in its supervisory process to determine an appropriate mix of on- and off-site supervision. In those instances where the SFBC perceives an institution exhibits a higher risk profile (in individual and/or systemic risk), greater emphasis should be on conducting an on-site inspection or analyzing information from the primary (in the case of insurance activities) or host (in the case of foreign operations) supervisors. Banks and securities firms are required to report to the SNB and SFBC their annual figures within 60 days of year-end ("early-information," see SFBC-Circular 99/3 Early Information). Based on this data, the SFBC carries out a peer group analysis and decides on measures where necessary. The SFBC is a member of various international financial working groups that monitor trends and developments and establish new principles on issues of concern to the banking industry on a global basis (e.g., the Basel Committee on Banking Supervision, the Joint Forum on Financial Conglomerates, FATF, and others). Participation in such groups has allowed the SFBC to keep in the forefront of emerging banking trends/issues. One example is in Internet only banks. The SFBC has licensed five such banks. Staff required E-Bank specific information and addressed a letter to all banks on March 29, 2001 on opening accounts in Internet exclusive banks and know-your-customer rules. SFBC staff monitor compliance with prudential ratios off-site through the monthly and quarterly returns received from the banks; staff take follow-up action where appropriate. In addition, the on-site inspection process includes checks for compliance with prudential reports and regulations. The SFBC has an internal rating system (A, B, C) for the Swiss banks. The SFBC management receive a complete list of "C" (i.e., problem banks) annually and is immediately informed on an individual basis of any significant event concerning these problem banks. Management is also kept informed of any earnings, organizational or operational problems at any of the banks. The goal of SFBC management oversight of the on-site and off-site inspection processes is to ensure the effectiveness of the on-site and off-site processes. Regarding on-site inspections, the external auditors are viewed by SFBC as doing a thorough job. They produce an inspection report that is provided to bank management and the SFBC. Where appropriate, issues are brought to the attention of the Board of the bank and senior management at the SFBC. Although the process of report review and meetings with the external auditors generally works, a more formal quality control or quality assurance program for overseeing and verifying the work of the external auditors is needed. There is no routine process in place to verify the information in the Long Form audit report. Since the SFBC authorizes the firms, continual oversight of the firms is necessary in order for the SFBC to ensure its supervisory role, outsourced to the auditors, is being properly discharged. This has also been recommended by one of the expert groups reviewing the Swiss supervisory system. Regarding off-site work, more could be done in compiling and using the data for supervisory purposes. However such reports can't take the place of regular meetings and contact with bank management. Any issues arising regarding prudential ratios and/or supervision requirements are identified by SFBC staff as well as changes to an institution's business profile/management structure. Although the SFBC does not have a specific legal mandate to share banking information with the Swiss insurance supervisor in financial conglomerate groups (such as CS Group), the lack of a legal mandate has not prevented sharing information useful to the assessment of the conglomerate. Even

	in the absence of a clear legal basis, the two supervisory agencies share information necessary for the supervision of the banking conglomerates. This includes customer data to the extent that this information is necessary for the purpose of consolidated supervision and is kept confidential. However, a clear legal basis for such information sharing is desirable. SFBC staff may not disclose any information concerning the business of any of the institutions under the SFBC's supervision unless such disclosure is permitted by law. Generally, non-disclosure requirements are waived if information is needed by and communicated to another domestic or foreign supervisor involved in financial institution supervision and such information disclosed will be held confidential by those other supervisors. The SFBC's supervision of credit institutions includes an in-depth understanding, periodic analysis and evaluation of individual banks, focusing on safety and soundness, based on meetings with management and a combination of both on-site and off-site supervision. The SFBC, through the external auditors on-site inspections, verifies that adequate corporate governance (including risk management and internal control systems) exists at individual banks; determines that information provided by banks to the SFBC and the public is reliable; obtains additional information needed to assess the condition of the bank and uses off-site work to review and analyze the financial condition of individual banks using prudential reports, statistical returns and other appropriate information, including publicly available information; and monitors trends and developments for the banking sector as a whole. Off-site and on-site work is prioritized based on the results of an assessment of the nature, importance and scope of the risks to which individual banks are exposed, including the business focus, the risk profile and the internal control environment.
Assessment	Compliant.
Comments	The Swiss authorities need to take the following actions: (1) formalize a quality assurance process for supervision of the external auditors to ensure the SFBC's mandates are being followed; (2) obtain sufficient additional detailed data, for example, asset quality, and develop an early warning system; (3) consider a more detailed large bank risk profile that would utilize off-site data as well as information obtained from trilateral meetings with foreign supervisors, insurance supervisors, management and external auditors; and (4) step up on-site supervision.
Principle 17.	**Bank Management Contact** Banking supervisors must have regular contact with bank management and a thorough understanding of the institution’s operations.
Description	Also see CP 16. The supervisory function is effected through a combination of both off-site surveillance and on-site inspections. Off-site surveillance involves the examination of detailed prudential/statistical returns received from the credit institutions on a monthly, quarterly, semi-annual and annual basis. On-site exams are done by external auditors within the scope developed jointly between the SFBC and the external auditor and focuses on asset quality, large exposures, capital, liquidity, corporate governance and internal controls and compliance with laws, etc. External audits are complemented by regular review meetings with senior management of the credit institutions (quarterly or monthly if necessary with the two large bank groups and on a rotating basis for the other banks (about 1/3 per year have a general meeting with the SFBC staff to discuss their individual bank)). Particularly in regard to the large banks, the interaction between the SFBC and bank management is excellent. Consideration should be given to implementing a process with the other Swiss banks whereby SFBC staff meets with management annually, possibly in conjunction with completion of the annual external audit and receipt of the Long Form report. The SFBC has a supervisory program in place that includes regular meetings with bank management, external and internal auditors and foreign country supervisors where appropriate. Quarterly meetings at the large banks address operational matters including strategy, group structure, corporate governance, performance, capital adequacy, liquidity, asset quality and risk management systems. The SFBC staff and management are very familiar with their institutions, including corporate structure, condition, and business activities. Staff remains current through

	review of the Long Form audit report, prudential report analysis, meetings with management and external auditors. The SFBC must be notified immediately by the banks and the external auditors, per the Banking Act and Banking Ordinance, of any violations or noncompliance with the approved business plans of the bank's license. Moreover, all changes to business activities must be incorporated into a bank's bylaws which require the approval of the SFBC. The fitness and propriety of bank management is always considered in granting a license and in supervising the bank once it commences business.
Assessment	Compliant.
Comments	Consideration should be given to implementing a process with the all Swiss banks whereby SFBC staff meet with management annually, possibly in conjunction with completion of the annual external audit and receipt of the Long Form report. Contacts with management of the two large banks should be more frequent.
Principle 18.	**Off-Site Supervision** Banking supervisors must have a means of collecting, reviewing, and analyzing prudential reports and statistical returns from banks on a solo and consolidated basis.
Description	See CP 16. Banks are subject to periodic reporting requirements (see also SFBC-Circular 92/1 of September 24, 1992, Matters Requiring Approval and Notification for Stock Exchanges, Financial intermediaries, Securities Dealers and Bank Auditors). A number of these reports encompass a range of financial data that are required for statistical and monetary policy purposes and thus must be submitted to the Swiss National Bank on a monthly, quarterly or annual basis. Other data is necessary for prudential purposes and is prepared on a solo and consolidated basis depending on the bank. The Banking Act and Banking Ordinance provide the legal authority for the SFBC to request information on a periodic basis from the banks. The reports vary in frequency but include own funds information, BIS equity statements, liquidity statements, large exposures, risk diversification information, annual reports and interim financial statements, early information following year end of income statement analysis, own funds data and supplementary data on a solo and a consolidated basis. Banks are also required to notify the SFBC of changes in controlling owners and business activities and bylaws. The annual Long Form external audit report provides detailed financial statement information that addresses all asset and liability categories in addition to other data. The Banking Act and Banking Ordinance provide the authority for the SFBC to implement additional rules/guidelines regarding the consolidation of accounts as well as accounting techniques. (See CP 21 for the assessment on accounting.) International Accounting Standards (IAS) and U.S. Generally Accepted Accounting Principles (US-GAAP) are considered to be equivalent to Swiss Financial Statement Reporting Provisions for banks. Banks organized in accordance with Swiss law which are under the controlling influence of persons with residence or registered office in an European Economic Area (EEA) member country may prepare their annual financial statements in accordance with the applicable provisions in their country of origin. Material deviations from the provisions of the Banking Ordinance and SFBC Guidelines of those international standards of financial statement reporting applied must be disclosed and detailed in the Appendix to the financial statements (see SFBC Guidelines concerning the provisions governing the preparation of financial statements, 29a-c). The SFBC has the power and the legal authority to enforce compliance with the requirements that information be submitted on a timely and accurate basis. In the event of material misreporting, the SFBC can require republication and pre-clearance of future filings until such time as they are confident that the filing bank will not misrepresent the financial data again. The SFBC and the SNB have standardized reports that must be filed by all banks. Details of the contents of the reports are either contained in the blank copy of the reports or in RRV-SFBC guidelines on Financial Statement Reporting dated December 14, 1994. Asset quality information is provided annually in the Long Form report for the general population of banks. Balance sheet information is provided monthly. The SFBC has the authority (per the Banking Act and Banking Ordinance) to request and receive all

	information deemed necessary to properly supervise the banks in Switzerland. The SFBC has staff responsible for reviewing and analyzing the prudential data filed and using it to supplement the annual Long Form external audit report. Using the information to establish peer group data to compare similar institutions would be an additional off-site tool for the SFBC and contribute to an early warning system. Prudential reports are collected from all banks and provided on a comparable basis. The prudential reports for the large banks are obtained on a monthly or quarterly basis, which is appropriate based on the higher risk profiles of these two institutions. Reports from smaller less complex banks are collected quarterly, semi-annually or annually depending on the type of information being collected.
Assessment	Compliant.
Comments	
Principle 19.	**Validation of Supervisory Information** Banking supervisors must have a means of independent validation of supervisory information either through on-site examinations or use of external auditors.
Description	See CP 16 regarding the use of licensed external auditors. While the SFBC is authorized by law to conduct on-site inspections, it does not generally perform such examinations itself. The staff of the SFBC holds meetings with senior bank management to discuss prudential issues or issues of supervisory concern. On-site inspections, including unscheduled audits, are carried out by the banks' external auditors on a regular basis. The costs incurred for such audits are paid for by the banks. In Switzerland, the use of independent though non-governmental external auditors is a primary tool for bank supervision. The responsibility of external auditors not only encompasses an audit of annual accounts but also entails a review of the bank's compliance with all prudential requirements, including due diligence rules (see SFBC Circular 96/3 Audit Report Form and Content). Thus, external audit firms can be seen as performing a quasi-governmental function, since they are required by law to inform supervisory institutions, and specifically the SFBC, of any violations or practices that have the potential of placing depositors' funds at risk. In 1999 external auditors charged 228,441 hours for the audit of the large financial intermediaries and 360,714 hours for all other financial intermediaries. While the appointment of external auditors is the responsibility of the directors of each bank, an audit firm must be selected from a list approved by the SFBC. By the end of 2000 eleven audit firms were approved and licensed. Approval criteria include the overall reputation and professional competence of the firm and its independent status. To be deemed independent, an approved audit firm must regularly audit at least five banks, and the firm's compensation from any one mandate must not exceed 10 percent of the firm's total fee income. The replacement of an audit firm by a bank is subject to approval by the SFBC. The bank has to indicate the reasons for the replacement. The SFBC also has the authority to require additional audits. For instance, in January 2001, the SFBC asked that banks with establishments in foreign financial centers commission their external auditors to perform an in-depth examination of the adequacy of their procedures, systems and controls governing anti-money laundering in meeting the requirements of the SFBC Guidelines. The scope of these examinations covered the adequacy and effectiveness of customer identification procedures, the functioning of internal control mechanisms and the communication and cooperation between internal audit and external audits. In addition, the auditors were required to report any indications that the foreign establishments may be used to circumvent Swiss legal requirements and professional rules. The in-depth exam was to be conducted by Swiss auditors familiar with the SFBC's and SBA's due diligence agreement and guidelines for such activities. Besides the in-depth examinations which fall within the scope of regular consolidated supervision activities required by Swiss law, the SFBC itself may mandate special audits to further investigate suspected shortcomings or irregularities or to verify the implementation of corrective measures or organizational improvements in particular banks. In the past year, the SFBC had comprehensive investigations conducted in several banks, which entered into business relations with the entourage

	of the former president of a foreign country and found serious omissions and organizational shortcomings in some. In order to establish whether these banks had corrected the identified irregularities and verify compliance with know-your-customer rules and policies regarding business relationships with politically exposed persons ("PEP rules"), the SFBC in August 2000 ordered a special audit to be carried out by an independent auditing firm, which included establishments of Swiss banks both within and outside of Switzerland. The auditors' specific tasks will consist primarily of reviewing the organizational structure and policies regarding the acceptance of clients, the account-opening procedures and the monitoring of accounts and testing of adherence to relevant internal control procedures, including a sampling of individual client files to assess compliance with due diligence requirements. The responsibility of external auditors not only encompasses an audit of annual financial statements but also entails the review of the banks' compliance with all prudential requirements (compliance with licensing requirements, due diligence rules, and the like). The assignment of the external auditor is not limited to the reporting of audit findings to the bank and the SFBC. In the event that the audit reveals either the violation of a legal provision or any other irregularity, the external auditor has to set an appropriate deadline for the bank to take corrective action. The external auditor must inform the SFBC if the correction is not carried out within the prescribed deadline (Art. 41 of the Banking Ordinance). Where the setting of a time limit appears of no use, or where the external auditor discovers a criminal offense, serious violations, or losses reducing the capital funds by 50 percent, or other irregularities jeopardizing the creditors' interests, or where it can no longer be affirmed that all creditors claims are still covered by the assets, the SFBC must be informed immediately (Art. 21 of the Banking Act). The role of the external auditor in the Swiss supervisory system is more comprehensive than the role of a bank's external auditor as described in §§ 15-28 of a joint paper issued by the Basel Committee on Banking Supervision and the International Federation of Accountants (IFAC) on "The relationship between banking supervisors and banks' external auditors." However, the criteria regarding additional requests for the auditor to contribute to the supervisory process laid down in the mentioned paper of the Basel Committee and the IFAC (§§ 57 – 68) are respected in the Swiss system. The Banking Act requires that, as part of their annual examination, auditors perform one or several interim examinations on a surprise basis to ascertain the existence of the bank's assets and the reliability of its records. Art. 40 of the Banking Act requires that the external auditors also perform unannounced interim examinations. Each year, in addition to the ordinary audit, the external auditors perform an in-depth examination of at least one area that is significant to the activities and risks of the bank. The SFBC supervises licensed audit firms and issues guidelines for conducting the annual bank audits and the form and content of the resulting audit report (frequently referred to as the "Long Form" report) (see RRV-SFBC dated December 14, 1994 and SFBC-Circular 96/3 dated October 21, 1996). SFBC staff maintains regular contact with the banks' external auditors and participates in bilateral and trilateral meetings with the auditors and the banks following completion of the annual Long Form report and at other times when setting the scope for special, follow-up or the next year's on-site exam. SFBC officials may meet with external auditors to discuss the audit report, even without the presence of bank officials and without the approval of the bank. Pursuant to Art. 46 of the Banking Act, a recognized bank auditor who intentionally violates the duties assigned to him/her by the Banking Act or the Banking Ordinance, for instance, who makes untrue statements in the audit report or omits essential facts, fails to request pertinent information from the client or fails to report all findings to the SFBC, can be punished by a prison term not exceeding six months or a fine. Moreover, the SFBC will withdraw the lead auditor's and firm's license preventing them from conducting further bank audits in Switzerland. Whenever major irregularities are found in an institution, the SFBC will initiate a procedure against the bank in order to establish whether any breaches were committed. In addition, the SFBC will initiate a procedure against the bank's external auditing firm to establish whether or not it has

	violated the requirement to perform the audit with the "care of a properly qualified auditor" (Art. 20 par. 4 of the Banking Act). As such, in the year 2000 the SFBC conducted a procedure with respect to the application of proper care in the audit of the global compliance function of an internationally active banking group (see SFBC's Annual Report 2000, pp. 47- 49). Following significant losses of the UBS business unit, Global Equity Derivatives Business (GEDE), in 1997/98, the SFBC also examined whether or not the external audit had carried out its audit mandate with the proper care. The SFBC found structural and organizational shortcomings in the exercise of the audit by the external auditor (SFBC's Annual Report 1999, p. 55). In another case the SFBC found that the external auditor failed to report certain violations of competence rules and insufficient credit documentation. The SFBC filed charges against two of the responsible chief auditors. (SFBC's Annual Report 1996, pp. 39-42). In another case, the SFBC initiated a procedure because the external auditors had reported irregularities to the bank management, but failed to report them to the SFBC as required (SFBC's Annual Report 1995, pp. 37-38). The most severe sanction the SFBC can take against an external auditing firm is the withdrawal of its recognition and license pursuant to the Banking Act. There are cases where the SFBC withdrew the recognition for non-fulfillment of recognition requirements as laid down in Arts. 35 and 36 of the Banking Ordinance (see, e.g., SFBC's Annual Report 1997, p. 55). In one case upon threatening to withdraw the recognition due to shortcomings in the audit performance, the auditing firm itself surrendered its recognition. The SFBC has sufficient legal authority to have bank information verified and to use external auditors to perform that function. The only possible exception to the process is the lack of a formal quality assurance program for supervising the work of the external auditors. Such a program is necessary given the key reliance placed on the external auditors.
Assessment	Compliant.
Comments	A formal quality assurance program for supervising and verifying the work of the external auditors is should be developed and implemented. Such a program seems necessary given the reliance placed on the external auditors.
Principle 20.	**Consolidated Supervision** An essential element of banking supervision is the ability of the supervisors to supervise the banking group on a consolidated basis.
Description	Due to increased concerns by the SFBC on the growing size and complexity of the two big Swiss banking groups, a new department was created in 1998 to strengthen supervision of these banks. The separate Large Bank Supervision unit is responsible for the ongoing monitoring of the two large banks, both at a group level and the single subsidiary level. The new program includes regular periodic visits of the two banks foreign branches and subsidiaries, on-site reviews domestically and abroad, and trilateral discussions with host country supervisors and with group management, external auditors and recently with staff from the Swiss Federal Office of Private Insurance (FOPI). The SFBC's authority is contained in the Banking Act and implementing Banking Ordinance. In 2001, the SFBC supervised 84 groups of banks on a consolidated basis, among these UBS and the Credit Suisse Group. The SFBC has an established practice for supervising banking groups, although the legal provisions for this consolidated supervisory task imposed on banking groups can be inferred from the general authority contained in the Banking Act and the Banking Ordinance, the current practice could be more clearly codified. Supervision of banking groups and financial conglomerates has become increasingly important and a more coherent set of rules should be put in place. Currently, a draft proposal for an amendment of the Banking Act and the SESTA (securities law) provides for a more comprehensive set of legal rules for the supervision of groups of banks and/or securities dealers as well as financial conglomerates are being brought before the Federal Council. If these amendments should pass Parliament, this would clarify the existing practice of the SFBC and provide it with a clear basis to coordinate its action with other regulators in the case of internationally active market players. Since there is no legal definition of a banking group in the Banking Act or the Banking Ordinance,

	whether or not to force groups to submit to supervision by the SFBC on a consolidated basis is not totally clear. Where the parent company holds a banking license, the requirement and scope of consolidated supervision is clearly circumscribed in the law (see provisions relative to consolidated capital requirements, Art. 13a Banking Act, 14 Securities Act, risk diversification rules on consolidated basis, Art. 21m Banking Ordinance, and consolidated financial statements, Art. 25e ff Banking Ordinance and SFBC-Circular 31ff). A loophole exists in the case of a financial group or conglomerate where the parent institution does not hold a banking license. This shortcoming is being addressed by a proposal for an amendment to the Banking Act and Securities Act, which was finalized in November 2001. The proposal establishes the supervisory competence of the SFBC relative to a financial group/ conglomerate that controls a Swiss bank or is being directed from Switzerland. The proposal lays down principles for the coordination of oversight functions in case of overlapping cross-sectoral and/or cross-border competencies. The proposal further sets forth, among other things, requirements regarding the "fitness and propriety" at group management level, adequate organization and risk management, accounting, auditing and reporting to the SFBC. The SFBC has the power to define specific requirements, for example, regarding capital and risk diversification. The SFBC imposes a regime of consolidated supervision on banking groups if their activity apart from that of its licensed bank(s) in the financial sector is of certain importance for the whole group and if it is impossible to have a fair view of the relevant financial risks by looking solely at the licensed bank(s). In a decision of February 26, 1998, concerning the Credit Suisse Group, the SFBC established formal duties of a financial conglomerate, which do not formally fall within the scope of the Banking Act. Credit Suisse Group was, among other things, required to comply as a group with capital and large exposure requirements, ensure adequate levels of liquidity of all members of the group and group-wide compliance with all the SFBC reporting requirements, the fitness and propriety and adequacy of the management of all group companies. In addition, the SFBC applies the requirement of fitness and propriety to persons in charge of the administration and management of banking groups in accordance with Art. 3 par. 2 lit. The Banking Act not only applies to banks but also to banking groups as well. This is the case even if the structure on top of a banking group is a not a licensed bank. However there appears to be a gap in the overall consolidated supervision of Credit Suisse Group relating to its insurance activities. These activities account for almost 25 percent of group earnings and yet the Swiss insurance supervisor purportedly is restricted by law from sharing confidential supervisory insurance relevant information with the SFBC absent a written agreement. As a result, the SFBC has persuaded both Credit Suisse Group and Winterthur insurance sub-group that it needs risk related information directly from its insurance activities. While the practice has worked successfully for the last two years, a clear legal basis for information sharing across financial sectors should be pursued. The host country bank supervisors in the United States and the United Kingdom acknowledged their review of the insurance activities of the group was very limited and that coordination in the United States with multiple state insurance regulators was in the early phases. Insurance supervisors have only recently begun looking at their supervised entities from a consolidated supervision perspective. With respect to the Credit Suisse Group conglomerate, SFBC large bank staff should evaluate the extent of the risk from the insurance activities of the group and immediately commence implementing better coordination efforts with insurance supervisors in major markets where Credit Suisse Group operates. Foreign entities are subject to the same prudential standards and audit requirements as their domestic parents. Therefore, a foreign affiliate of a Swiss bank may not decline to disclose information to Swiss supervisory authorities on the grounds that such disclosure is barred by local secrecy laws. In 1982, the Swiss Federal Court held that a Swiss bank with foreign-incorporated affiliates must be capable of providing the SFBC with all information that it deems necessary for supervisory purposes (BCE 108 II 519). A Swiss bank must neither circumvent Swiss due diligence rules (including the money laundering guidelines of the SFBC), nor place managers who fail the competence and fitness tests into key positions with affiliates aboard.

	Consolidated supervision, capital adequacy, and large exposure rules apply to all financial affiliates of Swiss banks whether domestic or foreign. Consolidated supervision and capital adequacy rules are applicable only to affiliated financial institutions and real estate firms. In general, a bank's ownership interest in a non-financial/non-real estate-related company does not involve the application of consolidated supervision or capital adequacy to the affiliated company. Large loan exposure limits are governed by provisions contained in Art. 21 of the Banking Ordinance. The new provisions on risk diversification became effective on December 31, 1997. The provisions on risk diversification are to be complied with both on a single-company and consolidated basis. Under specific circumstances, the SFBC may allow a certain relaxation—as defined in Art. 22 of the Banking Ordinance—or apply even stricter limitations. The SFBC requires the banks which it supervises as home-country regulator to report on a group-wide consolidated basis. If foreign regulations do not allow direct reporting to the Swiss based parent bank by the affiliate or branch, the SFBC requests information on affiliates and branches from the foreign host-country regulator (Art. 23^{sexies} of the Banking Act). If a complex financial group is not a financial conglomerate, that is, it only includes banks, securities firms, real-estate subsidiaries and financial companies but not insurance companies, capital adequacy is still measured on a consolidated basis and all subsidiaries are fully consolidated if they are majority owned or dominated and conduct financial activities. The Banking Act has a very broad interpretation of financial activities, which includes leasing, factoring, consumer credit, and asset management. Such activities qualify as "financial" and must be fully consolidated. The only exception to financial consolidation is historically the insurance business, which is not "financial" in the sense of the Banking Act and the Banking Ordinance. However, the investment in the company is risk weighted at 500 percent (5 times the Basel Capital Accord Minimum). Other non-financial activities, which are in the form of a participation, also require a 500 percent risk weighting. A banking supervisor is deemed to supervise on a consolidated basis if it receives sufficient information on the bank's worldwide operations, including relationships of a bank to any affiliate, to assess the overall financial condition of the bank and its compliance with laws and regulations. The SFBC ensures its banks have adequate procedures for monitoring and controlling worldwide activities through statutory and regulatory standards for operations that each Swiss bank must meet. Among these standards are requirements for adequate internal controls, oversight, administration and financial resources. The SFBC reviews compliance with these limitations on operations and with internal control requirements through an annual audit performed by an authorized/licensed external auditor. The SFBC may take supervisory actions that include requiring divestiture of a subsidiary in response to supervisory concerns. The SFBC obtains information on the condition of its globally active banks, their foreign offices and subsidiaries by requiring submission of periodic, consolidated financial reports and through the mandatory annual report by the external auditor. Generally, Swiss banks must consolidate for accounting purposes all foreign offices on a line-by-line basis and must include any majority-owned banking, finance or real estate subsidiary on a pro-rata or proportional accounting basis. The Banking Act requires Swiss banks to submit annual and semi-annual balance sheets and income statements to the SFBC. The SFBC also receives information regarding capital adequacy, country risk exposure and foreign exchange exposures from its banks annually. Information on risks (such as IRR) and inter-company transactions is received through large exposure reports that must be submitted both when such loans occur and annually. The SFBC evaluates prudential standards with respect to capital adequacy that effectively follows the risk-based capital standards of the Basel Accord. The Banking Act and Banking Ordinance prescribe the content of the mandatory annual report produced by a bank's external auditor. The auditor must review and report on a range of prudential issues and must express an opinion regarding compliance on a global consolidated basis with the conditions for licensing, accounting accuracy, risks, adjustments, undisclosed reserves, treatment of classified assets, fiduciary operations, exposures to single borrowers, insider lending, capital, liquidity, reserve allocation, foreign assets, internal controls and organization, and compliance with

	monetary controls. The Banking Act contains penalties to ensure correct reporting to the SFBC and external auditors face penalties for violations of their audit duties. Based on these facts, the SFBC is deemed to subject its banks to comprehensive supervision and regulation on a consolidated basis.
Assessment	Compliant.
Comments	A draft proposal for an amendment of the Banking Act and the SESTA provides for a more comprehensive set of legal rules for the supervision of groups of banks and/or securities dealers as well as financial conglomerates are being brought before the Federal Council. Passage of these amendments is recommended in order to clarify the existing practice of the SFBC and provide for a clear basis for the SFBC to coordinate its action with other regulators in the case of internationally active market players. SFBC supervises its banks on a consolidated basis but a potential gap was noted in its efforts to supervise the CS Group on a consolidated basis in light of the group's conglomerate status due to its significant insurance activities. The mission team recommends the large bank unit detail its risk profile for the group to account for the insurance activities. Efforts should begin as soon as possible to develop a strategy for ensuring insurance activities in major markets are adequately supervised.
Principle 21.	**Accounting Standards** Banking supervisors must be satisfied that each bank maintains adequate records drawn up in accordance with consistent accounting policies and practices that enable the supervisor to obtain a true and fair view of the financial condition of the bank and the profitability of its business, and that the bank publishes on a regular basis financial statements that fairly reflect its condition.
Description	Refer also to CP 20. Accounting practices, valuations and the preparation of balance sheet data are governed by the relevant provisions of the Swiss Code of Obligations, the Banking Act and its implementing Banking Ordinance, the guidelines of the SFBC. The accounting practices are meant to give a true and fair view of the financial position and the results of operations and cash flows. The listed nonbanking companies are required to disclose true and fair financial statements based on the Swiss-GAAP, the IAS or the U.S.-GAAP. The banking companies' financial statements are considered equivalent to these standards and are recognized by the Swiss exchange. All Swiss bank reporting is based upon the legal principles set out in the Code of Obligations which require that the financial statements be prepared according to Swiss GAAP and expressed in Swiss currency. The code, however, is modified and complemented by the Swiss banking regulations standards (RRV-SFBC issued December 14, 1994 and amended October 28, 1999, on Financial Statement Reporting Requirements) and means banks can, in a number of circumstances, report in adherence to IAS or U.S. GAAP. The SFBC may allow financial reporting to deviate from the guidelines if it is in conformity with recognized international standards (Art. 28 of the Banking Ordinance). The RRV-SFBC guidelines, influenced by EU accounting practices, now make Swiss financial statements more transparent and useful for investors and regulators as they clarify certain issues not dealt with in the Code of Obligations. The method for providing allowances is not specifically regulated; however, specific and general allowances are customary and disclosed in the notes to financial statements. Swiss accounting has changed significantly in the 1990s and bank reporting is now seen as closer to international standards. As a result, three different accounting standards are used in the published financial statements of banks. While most institutions use Swiss accounting standards, other international firms have adopted IAS, and other firms the U.S. Generally Accepted Accounting Principles (US GAAP). In other cases, institutions have maintained Swiss standards and reconciled them to US GAAP, for example, in order to facilitate listing on U.S. stock exchanges. But Swiss standards are less sufficient in the level of disclosure, particularly on asset quality. The SFBC is provided with additional non-public information in this area through the annual audit reports and the reporting (prudential returns) of the banks. However, it would be helpful in light of the growing internationalization of the Swiss financial system on the one hand and the progress toward a global set of accounting standards on the other, if the Swiss authorities were to encourage more detailed disclosure in their banks' financial statements.

	Prior to implementation, most of the SFBC's circular letters, rules and amendments to the Bank Act and Banking Ordinances are submitted to the Swiss Institute of Certified Accountants and Tax Consultants (an independent body for the country's external auditing firms) and the Swiss Bankers Association (SBA) for consultation. Once agreed upon, the changes to the Banking Act and Banking Ordinance will be officially promulgated. The SFBC publishes new or amended circulars. The Banking Act states that all banks must be audited annually by an independent audit corporation that is recognized by the SFBC. In order to be recognized by the SFBC as a bank auditor, the auditor must fulfill a number of requirements outlined in Articles 34-38 of the Banking Ordinance. The requirements pertain to a required capital structure of the audit firm, the integrity of the auditor's operations and professional certification. Both the audit firm and lead team auditor must be recognized in order to perform bank audits. An exception is made for the 537 Raiffeisen banks provided they have their own qualified audit department. They comprise 11 percent of the Swiss banking market with total group assets of SwF77.2 billion and equity of SwF3.5 billion. Pursuant to the Banking Act, all banks must prepare annual financial statements consisting of a balance sheet, income statement and an appendix. These statements are supplemented by an annual business report which details material events that occurred subsequent to the balance sheet date. Banks with total assets of at least SwF 100 million and whose off-balance sheet operations represent a significant portion of their business must also prepare a statement of cash flows as part of the annual financial statements. They must also prepare semi-annual interim financial statements consisting of a balance sheet and a profit and loss account. If a Swiss bank exercises control over one or more companies, it must prepare consolidated financial statements provided the activities of the companies are material. Swiss banks are required to disclose their annual reports in printed form within four months of the end of the business year. Banks are also required to publish their interim financial statements in the Swiss Official Gazette or other Swiss newspaper within two months of the end of the reporting period. The business reports must be made available to the press and any person requesting them. Auditing practices can vary from accounting firm to accounting firm. The Swiss Institute of Accounting Firms and Qualified Accountants provides considerable guidance. Standards applicable to the profession are incorporated in the Swiss Handbook of Auditing, which provides practical guidance. Regarding asset and liability valuation, the following items are noteworthy: – Loan classification: According to the guidelines of the SFBC, loans with interests that are more than 90 days overdue are considered as being at risk and thus non performing. The amount of the nonperforming loans is part of the direct reporting of the banks to the SFBC. The amount (and variation) of the allowances concerning impaired loans is part of the above-mentioned direct reporting and is indicated in the public annual financial statements. Depending on the accounting standards used, some banks may disclose nonperforming loans while others may not. – Swiss banks may not include interest past due more than 90 days in interest income. For loans more than 90 days past due, interest income recognition ceases and previous unearned interest income is reversed against current earnings. – Swiss banks may create both specific and general reserves for nonperforming loans subject to management discretion within limits set by law. – Pursuant to Swiss law, banks are permitted to consolidate the activities of insurance companies. The equity method of accounting is required for Swiss banks that exert significant influence over other companies and the bank maintains 20 percent or more of the voting capital of the subject entity. – Swiss banks are permitted to invest in non-financial companies up to a certain limit (a qualified participation may not exceed the equivalent of 15 percent of its equity and the total of such participations may not exceed 60 percent of equity). The material holdings are disclosed in the appendix of the public annual financial statements.

	Annual financial statements consist of the balance sheet, the statements of earnings and the appendix as detailed in Art. 23ss of the Banking Ordinance. Banks must issue annual financial statements and prudential reports on a stand alone and on a consolidated basis. International Accounting Standards (IAS) and U.S. Generally Accepted Accounting Principles (US GAAP) are considered to be equivalent to Swiss Financial Statement Reporting Provisions for banks. Banks organized in accordance with Swiss law which are under the controlling influence of persons with residence or registered office in an EEA member country may prepare their annual financial statements in accordance with the applicable provisions in their country of origin. Material deviations from the provisions of the Banking Ordinance and SFBC Guidelines of the international standards of financial statement reporting must be mentioned and quantified in the Appendix to the financial statements (see SFBC Guidelines concerning the provisions governing the preparation of financial statements, 29a-c). An external audit of banks' annual financial statements is mandatory. The responsibility of external bank auditors in Switzerland exceeds the audit of annual financial accounts. External bank auditors also must review a bank's compliance with all prudential requirements (compliance with licensing requirements, due diligence rules, etc.) in light of the Swiss dualistic bank supervision system. In order for an auditing firm and its lead auditor to perform a bank audit, both must be authorized and licensed by the SFBC. A bank must obtain the approval of the SFBC prior to changing its auditing firm or appointing one for the first time. The external auditor must prepare a report, commonly called the "Long Form," that contains the details required by the SFBC pursuant to SFBC Circular 96/3 dated October 21, 1996 with Amendments of August 26, 1999 and of October 28, 1999: Audit Report: Form and Content ("Audit Report"). Not only does the Long Form contain annual certification of a bank's financial statements, but it also contains detailed information on a bank's compliance with all requirements of the Banking Act, the Banking Ordinance, SFBC Circulars and Guidelines of the SBA. The Long Form is comprehensive and must be submitted to the SFBC. The annual Long Form plus any special audit reports requested from special exams are important tools for supervision by the SFBC. See CP 16 and 19 for further information regarding the role of the external auditor in the Swiss supervisory process, verification of records and on-site audits. The SFBC may hold bank management and the external auditors responsible for ensuring the accuracy and adequacy of the financial record keeping systems and timely filing of required reports. Annual reports likewise receive similar scrutiny for those banks required to file (non- deposit taking Private Banks, which are General Partnerships, are not required to produce or publish annual reports).
Assessment	Compliant.
Comments	
Principle 22.	**Remedial Measures** Banking supervisors must have at their disposal adequate supervisory measures to bring about timely corrective action when banks fail to meet prudential requirements (such as minimum capital adequacy ratios), when there are regulatory violations, or where depositors are threatened in any other way. In extreme circumstances, this should include the ability to revoke the banking license or recommend its revocation.
Description	Art. 23ter par. 1 of the Banking Act provides the required powers to the SFBC for taking an appropriate range of remedial actions against banks depending on the severity of a situation. These remedial actions are used to address such problems as failure to meet prudential requirements and violations of regulations. They range from informal oral or written communication with bank management to actions that involve the revocation of the banking license (Art. 23^{quinquies} par. 1 of the Banking Act). In addition to the powers mentioned above, under the Banking Act the SFBC has a broad range of possible actions, including: – suspending voting rights (Art. 23ter par. 1 of the Banking Act) and issuing an instruction to

	suspend dividend payments, – freezing the current activities of the bank, and – withholding approval of new activities or acquisitions. The SFBC is required to ensure that remedial actions are taken in a timely manner (Art. 23ter par. 2 of the Banking Act). However, the SFBC does not have the authority to publish enforcement activities, which have been imposed by them. The SFBC can order temporary measures, such as the suspension of bank directors and managers, which take effect immediately. However, there is no mechanism for the automatic imposition of administrative or penal sanctions. Under Swiss law, this requires the conduct of legal proceedings with the respect of all procedural guarantees. These penalties and sanctions may not only be applied to the bank, but, when and if necessary, also to management and/or the supervisory board. SFBC should have the authority to impose direct civil monetary penalties on banks or directors or managers on its own. In addition, Art. 23^{quater} of the Banking Act empowers the SFBC to delegate an expert to act as its observer in a bank if, because of misdemeanors, the claims of the creditors appear seriously jeopardized. The draft proposal on the amendment to the Banking Act delegate to this expert limited supervisory functions to act in a flexible way. The SFBC has no legal power to force a credit institution with material problems to merge with a healthier institution. However, the SFBC supports any solution more favorable than a piecemeal liquidation, such as initiating an acquisition or a merger. The proposed amendment to the Banking Act will streamline the existing regulation and codify the SFBC's current practices. In addition, the proposed amendment will explicitly empower the SFBC, for example, to bar, suspend or dismiss managers or directors, alter, reduce or terminate any activity that poses excessive risk, restrict an institution's business activities, or to impose temporary management along with reorganization measures. The draft law explicitly provides that a reorganization measure, such as a purchase and assumption transaction, does not require the approval of the shareholders assembly and thus may be imposed on unwilling shareholders.
Assessment	Compliant.
Comments	SFBC should have the authority to impose direct civil monetary penalties on banks or directors or managers on its own. In addition, the SFBC does not have the authority to publish enforcement activities that have been imposed by them. The proposed amendment to the Banking Act should cover both. Improvements are under way. An additional area where the SFBC would appreciate, and should have, clear legal enforcement authority is in their right to publish the identities of banks and individuals involved in money laundering activities and to impose monetary penalties for non-compliance with the money laundering law.
Principle 23.	**Globally Consolidated Supervision** Banking supervisors must practice global consolidated supervision over their internationally active banking organizations, adequately monitoring and applying appropriate prudential norms to all aspects of the business conducted by these banking organizations worldwide, primarily at their foreign branches, joint ventures, and subsidiaries.
Description	According to Art. 3 par. 7 of the Banking Act, banks organized under Swiss law shall notify the SFBC before they establish a subsidiary, branch, agency or representation abroad. Under Art. 23^{septies99} par. 1 of the Banking Act, the SFBC has the authority to supervise the overseas activities of locally incorporated banks. In this regard, Art. 7 par. 3, the scope of the bank's operations and their geographic terms shall correspond to its financial resources and administrative organization. In terms of the oversight of foreign entities and "fit and proper" bank management, these have to meet the same oversight requirement as is applicable to the head office of credit institutions. The SFBC has a policy for assessing whether it needs to conduct on-site examinations (through SFBC or external auditors) or require additional reporting, and it has the legal authority and resources to take such steps as and when appropriate. As mentioned above, under Art. 6b of the

	Banking Ordinance the SFBC can prohibit the foundation of new banking entities and can demand the closing of existing ones. The following describes the process by which consolidated supervision of international active banks is carried out in Switzerland: – The large banking group department regularly visits the local bank management (so far, mainly in the United Kingdom and the United States, exceptionally in other jurisdictions). The objectives are to be in touch with local management, make them realize there is a home regulator/supervisor, and for the Secretariat's staff to get to know the major businesses abroad. – On-site reviews consist of an audit-like visit in order to assess a previously well-defined area within one or both of the large banks. The review team is a joint legal and large banking department team. Such visits require a close coordination with the work of the internal and external audit. – Staff of the large banking groups department attends audits of external auditors. This is meant to improve the information level of the staff and to get an idea about the quality and the procedure of the external audit firm. Their attendance is mainly passive, thus not interrupting the work of the external audit. – The aim of meetings with foreign regulators is to share the same information and to achieve a common risk assessment. Moreover, the supervisory action plans are coordinated. The meetings have taken place so far three times a year in the three financial centers of Zurich, New York, and London. The meetings can also consist in the participation of a specific audit/inspection work of a foreign regulator. Beginning in the fall of 2001, the meetings have also been held on a less frequent basis in places like Singapore, Hong Kong, and Tokyo.
Assessment	Compliant.
Comments	
Principle 24.	**Host Country Supervision** A key component of consolidated supervision is establishing contact and information exchange with the various other supervisors involved, primarily host country supervisory authorities.
Description	The proper supervision of the foreign bank branches and subsidiaries in Switzerland, and Swiss banks' overseas branches and subsidiaries requires close international cooperation, ideally based on MoUs or letters of exchange. The SFBC has not signed any MoUs. Letters of exchange (compliance with rules and regulation of the respective country) have been signed with Denmark, the Netherlands, Sweden, and the United Kingdom. The exchange of information, cooperation and on-site visits are, in general, based only on informal arrangements. This could cause problems in conducting on-site visits in foreign countries with a higher frequency, as expected in the future, and after the implementation of the new Basel Capital Accord. A higher frequency of on-site inspections carried out by the SFBC makes it necessary, in the opinion of the assessors, to formalize this process through the conclusion of MoUs. However, such informal arrangements have not impaired the SFBC's ability to practice consolidated supervision in the past, including on-site inspections if necessary. As an outcome of the meetings with the Federal Reserve Bank of New York (FRB NY) and the Financial Services Authority (FSA) in the United Kingdom, the SFBC does not have direct contact with the U.S. SEC, which oversees the bulk of CSFB's U.S. operations. Instead, they deal with the FRB NY as the so-called umbrella supervisor. It is important that the SFBC establish a relationship with the primary supervisor of CSFB's U.S. operations. Neither the Fed nor the SFBC are closely monitoring the insurance activities of the Credit Swiss Group in the United States. The FSA acknowledges they are re-examining their insurance supervision Credit Suisse Group (24 percent of its income is from insurance). The FSA has recently started bilateral meetings with the Swiss insurance supervisor, but consolidated supervision is a relatively new concept for insurance supervisors.

	Under Art. 23^{sexies} of the Banking Act, the SFBC is empowered to provide information to host country supervisors, insofar as these authorities: – will use such information exclusively for direct supervision of banks; – are bound by official professional secrecy law; and – will not transmit this information to competent authorities or bodies which are entrusted with supervisory activities in the public interest without the prior consent of the SFBC or on the basis of a blanket permission contained in a treaty with a contracting state. As the establishment of operation in foreign countries requires approval by the SFBC, the Banking Commission has the power to reject any application where consolidated supervision would be hindered.
Assessment	Compliant.
Comments	Informal arrangements have not impaired the SFBC's ability to practice consolidated supervision in the past, including on-site inspections if necessary. The expected higher frequency of on-site inspections to be carried out by the SFBC would be facilitated if this process were formalized through the conclusion of MoUs.
Principle 25.	**Supervision Over Foreign Banks' Establishments** Banking supervisors must require the local operations of foreign banks to be conducted with the same high standards as are required of domestic institutions and must have powers to share information needed by the home country supervisors of those banks for the purpose of carrying out consolidated supervision.
Description	For branches and subsidiaries of foreign banks, the SFBC requires a license. These institutions are subject to similar regulatory requirements applicable to all other Swiss banks. Under Art. 3bis par. 1^{bis,} the SFBC requires that no objection or, preferably, the approval of the home country supervisor is received. In addition, the Banking Act provides some special requirements for foreign-owned banks that are similar to those for branches of foreign banks: – The country or countries where controlling shareholders are incorporated (or if the shareholders are individuals, the countries where they reside) must grant reciprocity to Swiss banks.[3] – If the Swiss bank is controlled by a foreign bank or other foreign financial institution, the parent must be subject to adequate supervision. Where no consolidated supervision exists by home-country authorities, the SFBC may impose specific reporting requirements for the Swiss entity in order to assure consolidated supervision. – The supervisory agencies of the parent's home-country must not object to the establishment of the subsidiary in Switzerland. – The bank must select a name that does not imply Swiss control. The SFBC requires all banks subject to its supervision as a lead home-country regulator to report on a group-wide consolidated basis. Conversely, Art. 4^{quiquies} of the Banking Act authorizes the Swiss-based affiliates (and branches) of foreign financial institutions to furnish information required for the parent institution's internal control purposes or for consolidated supervision by

[3] Reciprocity is, in most instances, an essential requirement for the licensing of any foreign bank entity including subsidiaries, branches, and representative offices. As a result, the issuance of a license generally will require that the home country of the applicant permit Swiss financial intermediaries to establish entities in that country with similar powers. However, the Banking Act provides that the requirement of reciprocity must give way to international treaty provisions such as the General Agreement on Tariffs and Trade (GATT). Thus, to the extent that GATT or other treaties call for different reciprocity standards, these will be applied to applicants whose home countries are covered by the treaty.

	their home-country regulator to their parent institution. The authorization is subject to three conditions: – the information may only be used for group-internal control purposes or for the direct regulatory supervision of the financial institution; – the parent company and the supervisory authority must be bound by official or professional secrecy; and – the information so obtained must not be forwarded to third parties without prior authorization by the Swiss affiliate unless generally agreed upon in a treaty (Art. 4^{quinquies} of the Banking Act). That information may also include customer-related information provided it is used exclusively for internal control and consolidated supervision purposes. Under Art. 23septies par. 2 of the Banking Act, the SFBC may permit foreign financial supervisory authorities to carry out direct inspections at Swiss establishments of foreign banks. Since the law was amended, foreign supervisors have conducted on-site examinations of foreign banks Swiss affiliates. Art. 23^{sexies} of the Banking Act give the SFBC the power to advise the home country supervisor on any material remedial action it takes.
Assessment	Compliant.
Comments	

Table 2. Summary Compliance with the Basel Core Principles

Core Principle	C[1/]	LC[2/]	MNC[3/]	NC[4/]	NA[5/]
1. Objectives, Autonomy, Powers, and Resources		**X**			
1.1 Objectives	**X**				
1.2 Independence		**X**			
1.3 Legal framework	**X**				
1.4 Enforcement powers	**X**				
1.5 Legal protection	**X**				
1.6 Information sharing	**X**				
2. Permissible Activities		**X**			
3. Licensing Criteria	**X**				
4. Ownership	**X**				
5. Investment Criteria	**X**				
6. Capital Adequacy	**X**				
7. Credit Policies	**X**				
8. Loan Evaluation and Loan-Loss Provisioning	**X**				
9. Large Exposure Limits	**X**				
10. Connected Lending	**X**				
11. Country Risk	**X**				
12. Market Risks	**X**				
13. Other Risks	**X**				
14. Internal Control and Audit	**X**				
15. Money Laundering	**X**				
16. On-Site and Off-Site Supervision	**X**				
17. Bank Management Contact	**X**				
18. Off-Site Supervision	**X**				
19. Validation of Supervisory Information	**X**				
20. Consolidated Supervision	**X**				
21. Accounting Standards	**X**				
22. Remedial Measures	**X**				
23. Globally Consolidated Supervision	**X**				
24. Host Country Supervision	**X**				
25. Supervision Over Foreign Banks' Establishments	**X**				

[1/] C: Compliant.
[2/] LC: Largely compliant.
[3/] MNC: Materially non-compliant.
[4/] NC: Non-compliant.
[5/] NA: Not applicable.

Recommended action plan and authorities' response to the assessment

Table 3. Recommended Action Plan—Basel Core Principles

Reference Principle	Recommended Action
CP 1.2. Independence	The SFBC should have full budgetary independence, based on the law.
CP 1.6. Information sharing	The SFBC should consider formalizing the exchange of information and on-site visits for example, through the conclusion of MOUs or the exchange of letters.
CP 2. Permissible Activities	An exception in the Banking Act (Art. 1 par. 2) permits nonbank employer-sponsored deposit-taking entities that are not licensed or regulated as financial institutions. This poses a risk to the system and should be eliminated.
CP 6. Capital Adequacy	The 12.5 percent capital reduction for cantonal banks should be eliminated on competition grounds.
CP 7. Credit Policies	Insufficient data is collected by the SFBC regarding renegotiated, past due, and internally classified credits. Such information, along with provisions, charge-offs, and recoveries, would be useful in monitoring asset quality trends in the banking system.
CP 13. Other Risks	Gap reports are not filed as part of the prudential reporting process and the current supervisory system for monitoring liquidity as part of off-site supervision is under review. The SFBC should continue investigating ways to improve its liquidity monitoring to align it with the Basel Committee's paper on managing liquidity in banking organizations.
CP 16. On-Site and Off-Site Supervision	Additional detailed data should be obtained (e.g., on asset quality), and an early warning system should be developed. Consideration should be given to setting up a more detailed large bank risk profile using off-site data and information from trilateral meetings with foreign supervisors, insurance supervisors, management and external auditors.
CP 17. Bank Management Contact	Consideration should be given to implementing a process with all Swiss banks whereby SFBC staff meets with management annually, possibly in conjunction with completion of the annual external audit and receipt of the Long Form report.
CP 19. Validation of Supervisory Information	A formal quality assurance program for supervising and verifying the work of the external auditors has to be developed and implemented. Such a program seems necessary given the reliance placed on the external auditors.
CP 20. Consolidated Supervision	A proposed amendment of the Banking Act, the Stock Exchange and Securities Trading Act, and the Insurance Supervision Act provides for a more comprehensive set of legal rules for the supervision of groups of banks and/or securities dealers as well as financial conglomerates. These amendments will be welcome. Further development of a strategy for supervision of insurance activities of Swiss conglomerates in major markets is recommended.
CP 22. Remedial Measures	The SFBC should have the authority to impose direct civil monetary penalties on banks or directors or managers and to publish enforcement activities. The proposed amendment to the Banking Act should cover both. An additional area where the SFBC should have, clear legal enforcement authority is in their right to publish the identities of banks and individuals involved in money laundering activities and to impose monetary penalties for noncompliance with the MLL.
CP 24. Host Country Supervision	Informal arrangements have not impaired the SFBC's ability to practice consolidated supervision in the past, including on-site inspections if necessary. The necessary higher frequency of on-site inspections to be carried out by the SFBC would be facilitated if this process were formalized through the conclusion of MOUs.

Authorities' response

In general, the Swiss authorities agreed with the main findings and the recommendations, in particular CP 1.2 (budgetary independence) and CP 2 (deposit taking entities). Most comments of the SFBC were included in the assessment. The main area in which the mission team identified a need for improvement and where agreement with the Swiss authorities was not fully reached is detailed below.

- CP 1.6/24: The SFBC shares the conviction that it is important to establish a relationship with other primary supervisors. As mentioned earlier, the existence of a formal co-operation arrangement with a foreign regulator is not a prerequisite for the exchange of information under Swiss law. While the existence of such arrangements may be useful in some cases, the SFBC finds that in the absence of such arrangements co-operation can be as efficient and oftentimes more flexible. There are no legal or other obstacles for the SFBC to enter into formal co-operation arrangements with a foreign counterpart. Should a foreign regulator, with whom the SFBC maintains close working relations, wish to formalize this process the SFBC does not raise any objections.

II. IOSCO OBJECTIVES AND PRINCIPLES OF SECURITIES REGULATION

This report was prepared as part of the Financial Sector Assessment Program (FSAP) of Switzerland. Its purpose is to assess implementation of the IOSCO Objectives and Principles of Securities Regulation.

An IMF mission visited Switzerland in October 2001 to conduct the assessment. The mission met with staff of the Swiss National Bank (SNB), the Swiss Federal Banking Commission (SFBC), the Swiss Exchange (SWX), the Swiss Funds Association, and several private sector firms. The assessment contained in this report is based on these discussions, on the responses to questionnaires sent to the SFBC, and on the analysis of relevant laws, regulations, administrative polices and other written information provided during the meetings.[4]

Institutional Setting and Market Structure

Supervision and regulation of the securities market are entrusted to the SFBC. The SFBC is responsible for licensing and supervising securities dealers and stock exchanges; it regulates disclosure of shareholdings in listed companies and takeover bids. Supervisory functions are also delegated to the exchanges, which function as SROs and supervise trading, exchange members and listing procedures.

As with the supervision of banks, the SFBC relies on recognized private external auditors to conduct front-line supervision and has not performed on-site inspections of securities dealers in the recent past. Front-line supervision of the SWX is also performed by an external auditor. The auditor is required to examine compliance with the obligations arising from the Stock Exchange Act, the implementing ordinance, and the relevant rules and regulations.

The SWX, as an SRO, is responsible for regulating its members and admitting participants to trading (who have to be licensed securities dealers); supervising price formation, execution and settlement of transactions; and ensuring that the information necessary "to maintain a transparent market" is made public. The Exchange is also responsible for enforcing listing rules and checking listing prospectuses.

In 2000, the SWX ranked 10th in the world by turnover in equities, with turnover of SwF1.0 trillion, more than double the turnover in 1996. Market capitalization of the Swiss Performance Index (SPI) was SwF 1.3 trillion at the end of 2000 (equivalent to three times annual GDP). Since June 2001, the stocks represented in the Swiss blue chip index (SMI) are being traded exclusively on Virt-x—the new pan-European blue chip exchange in London, which is a joint venture between the SWX and Tradepoint. The SWX is also one of the largest markets for warrants in the world with almost 3500 warrants listed. Since 1998, all Swiss standardized derivatives are traded on EUREX, which was created by the merger of

[4] The main author of the assessment was Nicoletta Giusto (CONSOB, Italy). The assessment is based on information available at the time of the FSAP mission in October 2001.

the Swiss Options and Financial Futures Exchange (SOFFEX) with the Deutsche Terminbörse (DTB).

Securities intermediaries comprise primarily securities dealers and investment funds.[5] Since the Swiss system is based on the universal bank model, both the securities and the fund businesses are dominated by banks. Total assets of investment funds have almost doubled since 1996 to SwF 468 billion (115 percent of GDP) at end-2000. More than two-thirds of the assets are invested in foreign funds, which are in most cases established by Swiss financial institutions in Luxembourg and their products are then offered in Switzerland to residents and nonresidents.

Principle-by-Principle Assessment

This section presents a detailed discussion and assessment of practices in Switzerland regarding securities regulation, vis-à-vis the practices in the IOSCO Objectives and Principles of Securities Regulation. The assessment of observance of each practice is made on a qualitative basis using a four-part assessment system: implemented; partially implemented; non-implemented; not applicable.

A Principle will be considered ***implemented*** whenever all assessment criteria are met without any material deficiencies. It will be considered ***partially implemented*** when the authorities have not fully implemented one or more assessment criteria. A Principle will be considered ***non-implemented*** whenever material shortcomings are found in adhering to the assessment criteria. When a principle is assessed to be partially or non-implemented, recommendations are provided to improve observance. A Principle will be considered ***not applicable*** whenever it does not apply given the existing structural and institutional conditions.

Table 4. Detailed Assessment of Observance of the IOSCO Objectives and Principles

Principle 1.	The responsibilities of the regulator should be clear and objectively stated.
Description	According to Article 23 of the Federal Law on Banks and Savings Banks, of November 8, 1934 (as subsequently amended), the Swiss Federal Banking Commission (SFBC) is responsible for the supervision of banks, securities dealers, investment funds, stock exchanges, the disclosure of significant participations, and public takeover bids. Details are provided in the Federal Law on Stock Exchange and Securities Trading (SESTA) of March 24, 1995 (as subsequently amended) and in the Federal Law on Investment Funds (IFL) of March 18, 1994. The above-mentioned laws do not include regulation of primary markets and of some asset management activities. A recently established commission of experts has a mandate to draft an oversight regime for asset managers.
Assessment	Partially implemented.

[5]The category of securities dealers includes not only market makers and client dealers (who trade securities in their own name for the account of clients), but also issuing houses and own account dealers.

Comments	The law sets out the responsibilities of the regulator—the SFBC. The scope of securities legislation, however, does not include all types of securities transactions or financial intermediaries and, as required by the IOSCO Objectives and Principles, regulation of primary markets. In particular, the jurisdiction of the SFBC does not include the regulation of (i) primary markets (details under Principle 14); (ii) asset managers or investment advisors who manage the assets of third parties only on the basis of powers of attorney, that is, they do not maintain accounts or security deposits in their own name for the account of these third parties; and (iii) closed-end funds.
Principle 2.	The regulator should be operationally independent and accountable in the exercise of its functions and powers.
Description	The Federal Law on Banking and Savings Banks (Banking Act) as supplemented by the Implementing Ordinance on Banks and Saving Banks of May 17, 1972 (as subsequently amended), establishes the procedure for appointing the members of the SFBC Board (the Commission), the mandate, and the incompatibilities. The Commission may consist of 7 to 11 members, appointed by the Federal Council (the Government), whose term is four years. The Federal Council appoints the Chairman and the Deputy Chairman (or Deputy Chairmen). The members need to be experts, presumably in the banking and securities field. The law establishes special incompatibilities for SFBC members. They cannot perform management functions or be chairman, vice-chairman, a delegated member of a board with executive responsibilities (or member of the executive committee of the board) of a bank, a fund manager, a stock exchange, a securities dealer, or a recognized auditing firm. However, SFBC members are allowed to perform other professional activities. The Federal Council, in consultation with the SFBC, appoints the Director and the Deputy Director of the Secretariat, and may remove an appointee in case of serious misbehavior. The Commission appoints the other employees. The Chairman of the Commission is responsible for handling general policy matters, running the Commission's meetings and supervising the Secretariat. The Chairman, as a general rule, does not get involved in the examination of individual cases. The Commission may delegate competences to the Secretariat and, in minor cases, can instruct the Secretariat to take decisions in its place. According to the relevant laws, the Secretariat is responsible for administrative and staff matters. It prepares the files for the Commission, makes proposals and implements the Commission's decisions. It carries out investigations and may deal directly with supervised entities. The decisions of the SFBC are subject to judicial review. The SFBC communicates with the Federal Council via the Federal Department of Finance. The SFBC must report annually to the Federal Council on its activities and must submit an annual report addressed to the Federal Assembly. The annual report is published. The Federal Council and the Federal Department of Finance may obtain special reports on demand. The SFBC has no budgetary independence and it is part of the central government budget. The SFBC's expenses are entirely covered by fees that are charged to institutions under its supervision. Proposals are under examination to grant the SFBC full administrative and budgetary independence from the Government.
Assessment	Partially implemented.
Comments	The SFBC does not appear to be fully operationally independent from the Government. Effective separation between the regulator and the government could be strengthened. The law could list in detail the cases when removal of the members of the Commission is possible. Currently, the law does not regulate in detail the procedure for the removal of the members of the Commission. The Commission's budget (see Principle 3 below) is part of the Federal Budget and therefore the SFBC has no budgetary independence.

	The Commission cannot deal directly with the Federal Council, and the intermediation of the Federal Department of Finance is necessary. The SFBC staff stresses that *de facto* the SFBC is independent, and that the Government has no legal basis to interfere with policy matters or individual decisions. Comprehensive rules on incompatibilities with professional activities could be established. The list of the forbidden activities is limited to certain managerial functions in supervised entities, and allows Commission members to perform other professional activities. If a conflict of interest arises in a particular matter, the member involved must abstain from participating and voting (the Federal Act on Administrative Procedure applies).
Principle 3.	The regulator should have adequate powers, proper resources and the capacity to perform its functions and exercise its powers.
Description	The SFBC has a staff of 115 (about 80 of which perform supervisory functions). There are no restrictions for SFBC staff to be employed by supervised institutions. The legal provisions applicable to Federal employees regulate the employment of SFBC staff, including their responsibilities. Civil liability claims cannot be addressed directly against the members of the SFBC or SFBC staff. The action must be brought against the Swiss Confederation. The private sector offers higher salaries, and SFBC staff is paid less than the staff of the SNB. The rate of staff turnover reached 18 percent in 2000. According to the law, the Commission, with the consent of the Federal Department of Finance, may deviate from the classification of a position in order to hire and/or retain particularly qualified personnel. The SFBC budget is part of the Federal budget; thus the use of resources must be approved by the Swiss Parliament. The SFBC, as part of the Federal Administration, is subject to audits by the Finance Control Office. The SFBC is funded through fees paid by supervised entities. The type and amount of fees are fixed in an ordinance issued by the Federal Council. Each authorized entity pays a basic fee and a turnover fee once a year. In addition, each time the SFBC issues a decision the concerned entity has to pay a decision fee. The SFBC is responsible for licensing securities dealers, investment funds, and exchanges. The SFBC powers can be summarized as follows. It can demand information and documents from (i) exchanges, institutions similar to exchanges, securities dealers, and investment funds; (ii) persons who hold a qualified participation in the capital of a stock exchange, a securities dealer or an investment fund; (iii) auditing firms; (iv) persons obliged to notify major holdings in listed companies; and (v) bidder and target companies subject to take-over regulations. The SFBC does not perform direct supervision on entities falling within its jurisdiction. Instead, it relies on external auditors, duly recognized, to perform front-line supervision of securities dealers, investment funds, and securities exchanges, that is, the SWX and Eurex Zürich. It maintains a list of auditors that are authorized to audit regulated financial intermediaries. The SFBC may issue supervisory orders requiring supervised entities to put an end to violations or other irregularities; suspend for a limited time all legal transactions and payments of (or due to) a securities dealer; bar the employees of a securities dealer from work (provisionally or for an unlimited duration). The SFBC may withdraw the license of a supervised entity. In cases where orders are not executed, the SFBC may take the necessary measures. The costs are born by the person or entity concerned. The SFBC, after having warned the concerned person, may publish its order and the fact that it was not complied with. According to the law, the SWX is responsible for regulating listed companies and supervising the market to detect market abuse practices. In case of suspicion, the exchange must inform the SFBC, which, in turn, can order the necessary investigations. The Takeover Board is responsible for administering takeover bids regulations. It refers violations and other irregularities to the SFBC.
Assessment	Partially implemented.

Comments	The independence of the SFBC in deciding about funding and resource allocation could be increased. The current process seems to be linked to decisions taken by the Government. Concerns have emerged about the ability of the regulator to retain skilled staff and reduce turnover. Furthermore, resources allocated to supervisory tasks seem to be inadequate given the size of the supervised securities and banking industry. The SFBC relies heavily on the front-line supervisory role played by external auditors. A more active involvement of the SFBC in direct supervision (including direct controls/on site inspections on the external auditors and their operations) would be advisable. The SFBC role in enforcing securities legislation could also be increased. Powers of investigation and enforcement in cases of market abuse (insider dealing and market manipulation) do not seem to be regulated in detail by the relevant legislation. The range of sanctions available to the regulator seems to be limited. The SFBC is working on a draft proposal (to be submitted to the legislator) that would broaden the set of available sanctions.
Principle 4.	The regulator should adopt clear and consistent regulatory processes.
Description	The SFBC consults extensively with the market before adopting new policies or new regulations. The legislation does not regulate formally this consultation process. Some regulations are drafted and proposed by professional associations (Swiss Bankers Association and Swiss Funds Association). If the SFBC approves the proposed regulation and endorses the proposed text, it makes the regulations binding. The decisions adopted by the SFBC are subject to judicial review. The SFBC does not organize investor education activities. The SFBC, however, publishes useful information on its website (http://www.ebk.admin.ch) and issues press releases, if necessary, to inform investors.
Assessment	Implemented.
Comments	It could be advisable, for the sake of transparency, to introduce formal rules on the consultation procedure with market participants and especially on the role played by professional associations. The issue of a possible conflict of interest when SROs and trade associations perform regulatory functions could also be addressed.
Principle 5.	The staff of the regulator should observe the highest professional standards including appropriate standards of confidentiality.
Description	The staff is subject to laws governing federal employees (including confidentiality obligations). Criminal provisions that punish misconduct by members of government agencies supplement these rules. The SFBC has also adopted a code of conduct that regulates financial transactions carried out by its members and employees. They must refrain from trading in securities issued by companies that are being supervised by the SFBC. There are no restrictions on future employment at supervised entities immediately after staff leaves the SFBC.
Assessment	Implemented.
Comments	Introducing restrictions on future employment, at least for senior officials, could be considered.
Principle 6.	The regulatory regime should make appropriate use of Self-Regulatory Organizations (SROs) that exercise some direct oversight responsibility for their respective areas of competence, and to the extent appropriate to the size and complexity of the markets.
Description	According to the law, formally only securities exchanges can be SROs. However, there are other bodies with regulatory functions in Switzerland such as the Takeover Board. This organization, which is a Federal Commission, is in charge of supervising takeover bids. The trade associations

	can also play a role in regulating securities markets on a voluntary basis. According to the law, the exchanges/SROs are responsible for (i) regulating their members and admitting participants to trading (who have to be licensed broker dealers); (ii) supervising price formation, execution and settlement of transactions; and (iii) ensuring that the information necessary "to maintain a transparent market" is made public. Exchanges/SROs are also responsible for listing rules. The law (Article 9) requires the SRO to establish an independent Board of Appeal. The right of civil action is unaffected. However, the civil action may be undertaken only after internal procedures have been exhausted. Exchanges/SROs should refer to the SFBC any irregularities and breaches of laws or of exchange regulations. The SFBC shall order the necessary investigations. However, the SRO retains the power of sanctioning its members. Imposed fines are regulated by civil law (as part of the contractual agreement between the exchange and its members). Presently, the SFBC has authorized only the SWX Swiss Exchange (SWX) and Eurex Zürich AG to act as SROs. The SWX is a nonprofit organization established as an association (according to article 60 of the Swiss Civil Code). Members have no claims on the assets or profits of the association. The purpose of the association is to operate an electronic securities exchange, and it may carry out other activities with the goal of improving and promoting the Swiss financial market. The SWX Swiss Exchange is part of the SWX Group, which includes participation in Eurex (derivatives exchange); EEX (European Energy Exchange); Virt-X; STOXX (a joint venture that offers indexes based on industry groups) and EXFEED (financial data). The Takeover Board is in charge of administering the regulations on takeover bids. According to the law, the Board is an independent body, not a SRO. The Takeover Board is set up by the SFBC. The Board comprises representatives of securities dealers, listed companies and investors. The Board does not have the power to issue binding decisions but can make recommendations. If these recommendations are not complied with, the Takeover Board informs the SFBC, which has the power to issue decisions. The budget of the Takeover Board is financed by the Exchange. However, the Takeover Board "may levy fees on the offeror and the offeree companies." The rules governing the activities of the SWX and of the Takeover Board must be approved by the SFBC. Professional associations—such as the Swiss Bankers Association (SBA) and Swiss Funds Association (SFA)—also play a role in drafting regulations and enforcing rules vis-à-vis their members. This role, however, is not formalized. Professional associations must report to the SFBC any serious irregularities committed by their members.
Assessment	Implemented.
Comments	The SFBC could play a more proactive and direct role in supervising the SWX, especially in the area of market surveillance and listing. In the area of admission to listing and supervision of listed companies, the role of the SFBC is to vet the rules (and the subsequent amendments) of the Exchange. On that occasion the SFBC may comment and ask for amendments. The SFBC is not responsible for the admission to listing of securities, nor for supervising the relevant disclosure obligations (initial, ongoing, and ad hoc disclosure obligations). The SFBC is still considering the regulatory treatment of ECNs or Alternative Trading Systems operated by authorized broker dealers or other entities for trading securities. For the sake of transparency and clarity in securities regulation, it might be advisable to regulate explicitly the regulatory functions performed by professional associations such as SBA and SFA.
Principle 7.	SROs should be subject to the oversight of the regulator and should observe standards of fairness and confidentiality when exercising powers and delegated responsibilities.
Description	The rules issued by the SWX (and the changes thereof) must be approved by the SFBC. The law sets the conditions for granting authorization to stock exchanges. For example, it mandates an internal organization that ensures the separation of certain functions, such as admission to listing,

	supervision, and management. The department responsible for listing admission must include representatives of issuers and investors. The SWX is governed by a Board of Directors; the general assembly of its members has a role in the approval of financial statements; ratification of the appointment of the members of the Board of Directors; removal of members of the Board for legally justified reasons; appointment of the auditors; approval of the annual membership fees; and decision on mergers, "de-mergers," and dissolution. At least four of the members of the Board are representatives of the major banks. The SWX has implemented the required separation of functions. The Admissions Board is responsible for issuing listing rules and for deciding on listing applications. It is composed of twelve members; five are nominated by the Swiss Federation of Trade and Industry, and seven by the SWX Board of Directors. The supervisory responsibilities entrusted to the SWX Swiss Exchange are discharged by the Supervisory Department, which is established by the Board of Directors. The appointment of the Head of the Supervisory Department is subject to prior approval by the SFBC. The Appeals Board is composed of three independent members and three substitutes (designated by the Board). The organizational structure, the rules of the procedure, and the nomination of the members are subject to approval by the SFBC. SWX employees and directors are subject to professional secrecy obligations. The rules adopted by the Takeover Board must be approved by the SFBC. The Takeover Board can issue recommendations. If the addressee does not comply, the SFBC has to be informed. There is the possibility to appeal to the SFBC. Incompatibility and obligations to abstain from participating in deliberations and voting are included in the rules approved by the SFBC.
Assessment	Implemented.
Comments	Given that the SWX is largely dominated by a few large private institutions, strong supervision by the SFBC may be needed to ensure adequate protection of end-users and investors, as well as the policing of possible market abuse practices. The SFBC's reliance on an external auditor may not be sufficient to ensure proper implementation of the Principle. In fact, according to the Principle, the regulator should be able to perform direct supervisory functions and to adopt directly relevant measures, when deemed necessary. The SFBC argues that it can exercise direct supervision whenever deemed necessary to enforce the Securities Act.
Principle 8.	The regulator should have comprehensive inspection, investigation and surveillance powers.
Description	According to the law, the SFBC has the legal power to demand information from supervised entities. It may carry out on-site investigations. According to the dualistic supervision model (see also Principle 3), the front-line supervision—both routine supervision and special examinations—is, however, performed by external auditors. The auditors must carry out at least one inspection per year on supervised entities and may perform interim audits if necessary. The external auditor has the duty to verify whether a securities dealer has fulfilled its legal duties and has complied with the licensing conditions. This verification is detailed in a report addressed to the SFBC. If, in the course of the annual or interim audit, violations or other irregularities emerge, the auditors must ask the securities dealer to put an end to the said irregularities and set a time limit. If the deadline is not respected, the auditor has to inform the SFBC. If violations or irregularities appear to be serious (or criminal activities are involved), the SFBC must be informed immediately. Exchanges and investment funds are supervised in a similar way (see Principles 6 and 7). The external auditors also play a role in examining licensing applications. Similarly, the regulations on takeover bids require external auditors to examine the conditions of the offer and the prospectus before the relevant documents are submitted to the Take-over Board. The SWX (acting as an SRO) must supervise trading in the market, including monitoring for insider dealing or price manipulation. The SWX, however, is not entitled to obtain information on

	securities dealers' clients (i.e., those who ordered the execution of the relevant transactions). Violations discovered by the SWX must be notified to the SFBC. The SFBC orders the required investigations. According to Article 11 of SESTA, it can instruct the stock exchange, an auditing firm, or other qualified individuals to conduct those investigations. The SWX is also responsible for the listing of securities and the disclosure of relevant holdings in listed companies. It can ask the respective external auditor to perform certain examinations of its members and of listed companies. The legislative framework does not clarify in detail which investigative powers are available to the SFBC concerning individuals and entities that are not subject to licensing requirements or obliged by law to report to the SFBC. The law (Article 51.b of the ordinance implementing banking legislation) authorizes the SFBC Secretariat and the members of the Commission to hear witnesses when necessary. This mechanism can be used to question individuals or entities, including those that are unsupervised. In this case, requirements set out in the Act on Administrative Procedure are applicable. Nevertheless, the scope of investigative powers vis-à-vis unregulated individuals/entities committing violations of securities is not clearly regulated. In performing its activities (including investigations), the SFBC must adhere to the rules set out in the Law on Administrative Procedure.
Assessment	Implemented.
Comments	The powers conferred to the SFBC could be strengthened. The SFBC relies heavily on the front-line supervision of external auditors or other bodies such as the SWX. In the first instance, it is up to the external auditors to decide how, if, and when on-site verifications should be carried out (apart from the general obligation to produce a report once per year). The fact that the front-line supervisory authority (the SWX) cannot directly investigate the person or entity that transmitted the order could delay market abuse investigations. It might be more effective to concentrate all the investigative activities directly in the SFBC. The legislative framework could also clarify expressly which direct investigative powers are available to the SFBC with respect to individuals or entities that are not subject to prudential supervision. The SFBC should be entrusted with formal surveillance powers on external auditors. At present, the only sanction available to the SFBC is to withdraw the auditor's recognition. According to the law, this measure can be adopted only when an auditor acts in violation of regulations ("grossly violates its legal duties"). There are no other intermediate measures available to the SFBC. The SFBC is considering how the independence of the auditor—who is paid by the supervised entity—could be reinforced, including by introducing a rotating mechanism for auditors. In Switzerland, there are currently 11 recognized auditors. However, only the major auditing firms are likely to be able to supervise large securities dealers (or the SWX). The Expert Commission on Bank Auditing has issued recommendations on the use of auditors. This Expert Commission emphasized the need of a more direct involvement of the SFBC in the examination process and a quality assurance program for the external auditors. External auditor reports should be closely examined by the SFBC even if they do not identify any violation by the supervised entity.
Principle 9.	The regulator should have comprehensive enforcement powers.
Description	The SFBC has the powers to order supervised entities to put an end to breaches of securities legislation, correct misbehaviors, and restore a sound organization. In case of non-compliance, the SFBC can decide, after having warned the concerned entity, to disclose to the public the relevant facts. The range of sanctions available to the SFBC includes (i) withdrawing the license from securities dealers, stock exchanges, and investment funds; (ii) imposing trading restrictions on securities dealers; (iii) ordering the suspension of payments by (or due to) a securities dealer when creditors (or debtors) may be damaged; (iv) appointing an observer if a securities dealer's or investment

	management company's governing body proves incapable of properly performing its functions; and (v) withdrawing the recognition of external auditors. In other cases, the SFBC must report to the authorities in charge of administrative and criminal prosecution (Federal Finance Department or cantons). Notably, this occurs when (i) securities activities for which a license is required are performed without a license; (ii) notification requirements on the acquisition or sale of relevant holdings in listed companies are violated; (iii) the takeover bid legislation is violated; or (iv) professional secrecy obligations are breached. Insider dealing and market manipulation are punished as criminal offenses. These offenses can be prosecuted directly by the SFBC under administrative law if regulated persons or entities are involved. Sanctions available in these cases are those described in general terms above (i.e., withdrawal of a license, and other sanctions). If the SFBC becomes aware of possible criminal acts (by regulated or non-regulated individuals/entities), it has the obligation to notify the competent criminal prosecutor. The SWX (as SRO) can enforce its rules and can fine its members or listed companies. The following measures are available: reprimands; suspension of participants or traders; imposition of fines up to SwF10 million; suspension of securities from trading (or delisting). These measures are classified as civil law measures. Entities affected by a SWX decision may appeal directly to the Appeals Board of the exchange.
Assessment	Partially implemented.
Comments	The type and quality of sanctions available in cases of securities legislation violations is relevant in evaluating the soundness of a supervisory system. The range of sanctions available to the SFBC is confined to supervised entities and does not provide for a sufficient ladder of available sanctions. The withdrawal of the license is a decision that, probably, would be adopted only when substantial violations have been committed. Violations of conduct of business rules probably will be punished by a simple order to avoid such misbehaviors in the future. Market abuse behaviors, such as insider dealing and market manipulation, if punished under criminal law require the prosecutor to be able to prove the intent to violate the law (as well as other elements of the criminal conduct). Since in many cases it is difficult to achieve such a level of proof, it can be difficult to sanction these illegal activities. The fact that certain violations can be sanctioned only under criminal law may make enforcement less efficient. In most jurisdictions, administrative sanctions are commonly used in those circumstances. The SFBC is working on a draft proposal aimed at broadening and strengthening the sanctions that can be imposed directly by the SFBC, including the power to impose monetary penalties. This project should be supported.
Principle 10.	The regulatory system should ensure an effective and credible use of inspection, investigation, surveillance and enforcement powers and implementation of an effective compliance program.
Description	As discussed under Principles 8 and 9 above, the SFBC does not normally perform direct supervision. Typically, it gets directly involved when complaints are lodged or information is received from the auditors that warrant its intervention. The auditors normally decide about the type of auditing activity they perform on supervised entities. The SFBC may give instructions. Particular attention is paid to the supervision of large banking groups, which are also active in the securities field. The SFBC does not publish supervisory programs.
Assessment	Partially implemented.
Comments	The implementation of this principle depends on the comprehensive evaluation of the supervision and enforcement system discussed under Principle 8 and 9. There are ongoing discussions between the external auditors and SFBC staff (at least in the case of the large internationally active financial institutions). The system, however, could be improved by more direct intervention by the regulator. The recommendations by the Expert Commission on the use of auditors were mentioned under Principle 9.

	Supervision could be more focused on compliance with investor protection rules. The core of the supervisory efforts appears to be addressed to verifying the financial soundness of the supervised entities more than their behaviors towards customers. Investor protection rules could be strengthened, for example through better disclosure. In the context of asset management (at least the regulated part), more attention could be paid to potential conflict of interest issues and suitability rules. The SFBC is in the process of drafting guidelines on market conduct.
Principle 11.	The regulator should have authority to share both public and non-public information with domestic and foreign counterparts.
Description	The law regulates the exchange of supervisory information, cooperation and mutual assistance (domestic and cross border). The relationship between the SFBC and the external auditors, or among the SFBC, the SWX and the Takeover Board, are regulated in detail by laws and implementing regulations. The banking law and implementing measures provide for some cooperation between the SFBC and the SNB. Cooperation with insurance and/or pension funds regulators is not regulated, but there is some of cooperation, especially in the supervision of financial conglomerates. Exchange of information with foreign regulators is governed in detail by legal provisions. The law distinguishes two cases: (i) confidential information concerning supervised entities, and (ii) confidential information on clients of Swiss intermediaries (banks, securities dealers, funds). In the case of confidential information concerning supervised entities, the information can be transmitted only if the foreign supervisor (i) "uses such information exclusively for the purpose of direct supervision of the exchange and the trading in securities"; (ii) is bound by official or professional secrecy; and (iii) does not, without the prior consent of the SFBC or by virtue of a general authorization clause in an International Treaty, forward such information to competent authorities and to other bodies, which carry out supervisory functions in the public interest. Forwarding information to criminal authorities is only permitted in the context of agreements on mutual assistance in criminal matters. The SFBC decides in consultation with the Federal Office for Police Matters if the recipient authority can use the information in the context of a criminal procedure. For the sharing of confidential information concerning clients of a Swiss intermediary, in addition to the above criteria, further requirements must be met. In particular, requirements established in the Federal Act on Administrative Procedure must be fulfilled. In accordance with that law, the SFBC must issue an order to the intermediary and to the client before it passes the information to the foreign regulator. If the client does not consent, he/she can appeal to the relevant Court, and the SFBC cannot communicate the information to the requesting regulator until (and if) the Court permits it.
Assessment	Partially implemented.
Comments	The Swiss legislation in this area is not fully in line with IOSCO standards and international practice. According to IOSCO standards, relevant information must be exchanged among regulators, domestically and internationally, without restrictions. Administrative cooperation among regulators should not be subject to restrictions and delays imposed by judicial cooperation, such as the need to wait for a Court decision. According to IOSCO standards the exchange of confidential information is a pre-condition for ensuring proper functioning of securities markets and effective law enforcement. The regulator should be able to communicate all types of confidential information in its own right without being obliged to wait for a Court decision. At the domestic level, the legislation does not provide for full freedom to exchange information with all concerned authorities (including those responsible for insurance and pensions), especially when individuals are involved. At the international level, for the exchange of confidential information concerning clients of Swiss intermediaries, an intervention of the Court is necessary. It is up to the Court to decide whether

	the information can be transmitted or not, and there have been cases when the Courts have ruled against such communication. The SFBC has publicly recognized that the Swiss law does not allow adequate cooperation with foreign regulators. It announced the intention to submit a proposal for amendment to the Federal Department of Finance. Swiss law can have other undesirable implications for cross-border investigations. The client of a Swiss intermediary must be informed of being under investigation by a foreign authority. If the individual goes to court, the investigation is publicly disclosed in the court proceeding. As a result, other targets of the investigation can adopt measures to avoid prosecution. The dual criminality requirement may also not be fully in line with international standards. According to Swiss law, information on supervised entities or on securities dealers' clients may be communicated by the regulator in the context of a criminal procedure only if the conduct is also illegal under Swiss criminal law. If the foreign definition of the illegal conduct is broader, the Swiss authorities may withhold their consent to use the information in a criminal procedure. Therefore, the foreign regulator who according to its legislation is responsible for assisting in criminal or administrative sanctioning proceedings, cannot use the information.
Principle 12.	Regulators should establish information sharing mechanisms that set out when and how they will share both public and non-public information with their domestic and foreign counterparts.
Description	The conditions for exchanging confidential information are established by law. According to the SFBC, therefore, there is no necessity for concluding memoranda of understanding (MOUs) between supervisory authorities. The SFBC has obtained declarations from supervisory authorities in 15 countries in which the relevant authorities commit to fulfill the conditions set out in Article 38 of the Federal Law on Exchanges and Securities Trading. Information can be transmitted to authorities in other countries with the previous consent of the SFBC. Consent from the Federal Police Office is necessary for the information to be used in a criminal procedure. Special agreements have been signed with regulators that are responsible for supervising exchange alliances, such as Virt-X and Eurex, or in case of remote membership.
Assessment	Partially implemented.
Comments	The restrictions on the international exchange of information and the procedures described under Principle 11 are applicable, irrespective of existing MOUs. Notwithstanding the special agreements for Virt-X and Eurex, the restrictions explained above under Principle 11 fully apply. This implies that if the U.K. or German authorities responsible for supervising the said regulated markets need information about clients of Swiss intermediaries (which are market members), they are subject to the rules described above. Therefore there is the danger that they are unable to properly enforce legislation against market abuse.
Principle 13.	The regulatory system should allow for assistance to be provided to foreign regulators who need to make inquiries in the discharge of their functions and exercise of their powers.
Description	The SFBC can provide information to foreign regulators on license holders, brokerage accounts, and disclosure of relevant holdings in listed companies (information on listed companies is available from the SWX). Other types of information on non-supervised entities or activities are available if it is verified through an investigation that Swiss law has been breached. The SFBC is under no obligation, however, to provide assistance to foreign regulators. Foreign regulators can only perform on-site inspections (or joint inspections) for the purpose of consolidated supervision.
Assessment	Partially implemented.
Comments	In addition to the legal restrictions examined under Principles 11 and 12, the ability of the SFBC to gather information on behalf of a foreign regulator could be limited by the fact that certain securities transactions and activities do not fall under securities regulations. As expressly recognized in the answers to the self-assessment questionnaires, the SFBC is not in a position to provide assistance in the case of boiler rooms activities, and in the case of information concerning

	individuals, since the restrictions explained under Principles 11 and 12 fully apply.
Principle 14.	There should be full, accurate and timely disclosure of financial results and other information that is material to investors' decisions.
Description	Public offers on the primary market are outside the scope of securities regulation. Few articles in the civil code regulate the matter. Remedies available are also limited to civil law. Therefore, the SFBC does not have the power to verify that the information published is accurate, and that all information material to investors' decisions is disclosed. There is no oversight of offering procedures, and the SFBC does not have the power to stop or delay offerings that may be prejudicial to investors. Investors have to rely on civil law remedies, for instance, bringing suit against the issuer. In case of public offerings for the subsequent admission to listing, the prospectus is to be drafted according to listing rules and once listed, the issuer is subject to supervision by the relevant SRO. The listing admission process falls within the jurisdiction of the exchange/SRO (the SWX). The rules are drafted by the SRO and must be approved by the SFBC (on the Admission Board of the SWX, see under Principle 7). Listing rules, which according to SFBC staff are in line with the European Listing Directives (79/279/EEC and 80/390/EEC), provide for initial, ongoing, and ad hoc disclosure requirements. Initial disclosure requirements include the obligation to publish a prospectus. However, the SWX allows securities to be listed without a Swiss prospectus if they have been previously listed on an official exchange recognized by the SWX. Under the listing rules the issuer must disclose all material information relevant to investors. The information must be presented in a way that is not misleading to prospective investors. However, the rules on the minimum content of the prospectus differ according to the type of securities (shares, bonds, derivative products), the type of issuer (large company, small cap, start up, high tech), and the segment of the market where the securities are traded. In case of small caps or start ups, additional information is required, as the SWX holds the view that more detailed information is necessary to allow investors to make informed investment decisions. As regards ongoing disclosure requirements, issuers of securities admitted to trading on the SWX must publish annual reports. Share issuers must also publish interim reports (on a semi-annual basis). Issuers listed in the SWX New Market segment have to provide quarterly reports. The SWX reviews the annual and interim reports. As regards ad hoc disclosure requirements, according to listing rules the issuer must inform the market of any not-publicly known fact that may result in "substantial" movements in the price of the securities. The issuer may postpone or omit disclosure if (i) the new facts are based on a plan or decision of the issuer, and (ii) its dissemination is liable to prejudice the legitimate interests of the issuer. Special rules deal with disclosure of shareholdings in listed companies. An owner who, directly, indirectly, or in concert with third parties, acquires or sells for his own account equities that represent certain threshold levels of the voting rights in a company listed in Switzerland must notify the company and the stock exchange where the company is listed. The SWX can refuse the admission to listing or can impose conditions that need to be met by the issuer before the securities can be traded. Sanctions can be imposed for violations, including reprimands, financial fines, suspension from trading, and delisting.
Assessment	Partially implemented.
Comments	According to the IOSCO Principles, securities regulation should include the primary market. The regulator should have the power to require (and enforce) the disclosure of all information material to investors' decisions. The regulator should also have the power to delay or stop an offer if investor protection is jeopardized. The relevant articles in the Civil Code do not require the issuer to comply with internationally

	accepted disclosure standards—see IOSCO Principles (chapter 10.4) and IOSCO International Disclosure Standards for Cross-Border Offerings and Initial Listing for Foreign Issuers. Since the primary market is not subject to supervision, the SFBC's (or the SRO's) powers do not extend to issuers that do not subsequently list on an exchange. From a legal viewpoint, also in the case of subsequent listing, the issuer will be subject to SRO obligations only in connection with listing. The SFBC does not have direct supervisory powers on listed companies. The responsible authority is the SRO (the SWX).
Principle 15.	Holders of securities in a company should be treated in a fair and equitable manner.
Description	Shareholders' rights are regulated under ordinary company law. According to company law, preferential voting treatment can be provided for certain categories of shares. There are no specific rules on corporate governance dealing with the rights of minority shareholders. The SWX has recently issued a consultative paper on good corporate governance practices, which focuses only on disclosure matters and proper conduct by board members, but does not cover rules on minority shareholders' rights (i.e., appointment of independent directors, members of the internal auditing committee of issuers) and collecting and exercising proxies. Only judicial authorities are responsible in case of appeals against decisions adopted at the shareholders' meeting. As described under Principle 14 above, there are rules obliging those who intend to acquire or to sell major holdings in a listed company to disclose their holdings. Also, rules exist on take-over bids applicable to Swiss companies whose shares are listed on a Swiss stock exchange. The law, however, applies only on a voluntary basis. In fact, according to Article 22 of the Federal Law on Stock Exchanges and Trading in Securities of March 24, 1995, a company may add to its by-laws, under specific conditions, even after having been admitted to listing, a provision that eliminates the obligation to launch a mandatory offer by those who intend to acquire the control of the company (the threshold is set at 33.3 percent). The only condition, in this case, is that the existing shareholders are not adversely affected. The Takeover Board may grant derogation in specific cases listed in the law. The offeror must publish the content of the offer and a prospectus containing all the relevant information. A recognized auditing firm must examine the bid prior to its publication to verify that the offer is in compliance with the relevant laws. The Board of Directors of the target company must issue a report on the proposed offer. After the publication of the offer and before the closing of the procedure, the Board of Directors of the target company must not adopt resolutions or acts that would significantly alter the assets and liabilities of the company. No restrictions are provided for decisions adopted by the shareholders meeting. These decisions may be executed irrespective of when they are adopted (prior or after the publication of the bid).
Assessment	Partially implemented.
Comments	The SFBC has limited competence in ensuring shareholder protection. The fact that a company may choose whether or not to be subject to takeover bid rules seems to be at odds with the IOSCO Principle, which requires that shareholders should be treated in a fair and equitable manner. The fact that it is stated in the by-laws that the law on mandatory take-over bids is not applicable does not ensure adequate investor protection. It simply means that the investor may know it. The legislative framework does not deal with the collection and use of proxies.
Principle 16.	Accounting and auditing standards should be of a high and internationally acceptable quality.
Description	The SFBC is not responsible for ensuring the quality of accounting or auditing standards. Professional bodies set accounting standards for issuers. The accounting standards employed in Switzerland are contained in the Swiss Accounting and Reporting Recommendations (ARR) drawn up by the Commission for Accounting and Reporting Recommendations. This Commission is an independent foundation.

	There is no supervisory body for the ARR. According to the Federal Law on Stock Exchanges and Trading in Securities, for listing purposes "the stock exchange shall take into account internationally recognized standards." The SWX, via listing rules, can require supplementary information or the application of different standards. According to the existing listing rules, the SWX—depending on the market segment—accepts financial statements drafted according to FER/ARR, IAS, US GAAP as well as financial statements of foreign companies prepared in accordance with the standards of their home countries. The SWX, in performing its supervisory functions, is advised by a panel of experts. The SWX may sanction listed companies that fail to report properly (i.e., who omit material information in their reports). The sanctions available include reprimands, fines, public disclosure of the violation, or deregistration. Auditors are not required to follow a published set of generally accepted auditing standards. However, the Swiss Institute of Certified Accountants and Tax Consultants (SICATC) publishes a set of standards. Members of SICATC are required to follow its standards. Auditors do not need to be approved or licensed except if they audit banks or securities dealers. However, auditors of listed companies must possess professional qualifications as defined by federal regulation and have to be registered with the SWX. Accountants who have passed an examination by the SICATC can be considered as "specially qualified" for auditing listed companies. Ongoing professional educational requirements and reviews to ensure that audit standards are applied properly are provided by SICATC for its members. Affiliation with the Institute is voluntary.
Assessment	Partially implemented.
Comments	The legislation in this area does not provide for a direct involvement of the SFBC in mandating and enforcing the application of international accounting standards. The SRO (the SWX), which is responsible for listing, accepts financial statements drafted according to defined principles. It is not empowered to check the contents and the quality of the principles. It does not have any input in standard setting bodies and is not involved in direct supervision of the auditors (it cannot sanction the auditors). The possible use of different accounting standards may affect the capability of the investors to compare (and properly evaluate) financial results of listed companies. There are no general mandatory requirements for qualifying individuals as accepted auditors of listed companies. There is no general supervisory system. Different bodies and entities are involved. Various assessments, including on an ad hoc basis, seem to be possible. There is no mandatory affiliation to a professional body. Violations of rules may entail different consequences depending on whether or not the auditor belongs to a professional association. The SFBC should ensure that in all cases (not only for financial institutions) the relevant accounting and auditing principles are of high and internationally accepted quality. Improvements in the supervision and enforcement of auditing standards are recommended, including the strengthening of auditors' independence.
Principle 17.	The regulatory system should set standards for the eligibility and the regulation of those who wish to market or operate a collective investment scheme.
Description	The Investment Funds Act of 1994 establishes the requirements for operating collective investment schemes in the form of the open-ended contractual type. Closed-end funds are not included in the scope of the law and are not subject to prudential supervision. However, if closed-end funds are admitted to listing, they are subject to disclosure obligations according to the relevant listing rules. This law is inspired by the EC Directive on UCITS (85/611/EEC), and it requires that the asset management companies be set up as independent entities whose sole business is to manage assets belonging to collective investment schemes. The assets belonging to each fund must be segregated

	and held in a bank (the custodian bank). Fund management companies are legally, personally, and functionally segregated from custodian banks, and their executive managers must be independent of each other. However, fund management companies are often subsidiaries of custodian banks. Custodians that check compliance with the fund's regulations normally belong to the same group (see below). The large financial institutions (UBS and Credit Suisse Group) dominate the fund business. The law is supplemented by the Investment Fund Ordinance and by the Code of Conduct of the Swiss Funds Association that has been endorsed by the SFBC. There are three type of funds: (i) securities funds (UCITS) with a traditional risk profile; (ii) other funds, including funds that have traditional risk profiles but that are not securities funds, and funds bearing special risks not comparable with securities funds' risks (including financial and commodity derivatives funds, and hedge funds); and (iii) real estate funds. Fund management companies must be authorized by the SFBC. A fund's rules, which must be submitted to the SFBC for approval, must contain, inter alia, provisions concerning investment policy (expressly mentioning special risks), calculation of issue and redemption prices, distribution of profits; managers' compensation, and fees and expenses. To be authorized, a company must fulfill capital adequacy requirements, and the executive management be fit and proper. Professional experience to perform the duties is required in all cases; but only in the case of special risk funds, at least two executive managers must possess thorough training in the field of the contemplated investments and have at least five years of business experience. The same persons cannot be managers of the fund management company and of the custodian bank. The names of those who, by virtue of the participation in the capital of the fund management company, are in a position to influence directly or indirectly the business activity of the company, must be notified to the SFBC. The management company must also possess an appropriate organizational structure. Termination or winding down of a fund must follow principles provided for in the law. Persons in charge of selling funds to the public must be authorized. Foreign funds must appoint a representative in Switzerland. The fund management company, the custodian bank, and affiliated parties and agents must operate in the exclusive interest of the unit holders. General principles have been established in the law and the implementing regulations. Detailed requirements are included in the Code of Conduct issued by the Swiss Funds Association and endorsed by the SFBC. The fund management company must maintain separate records for each fund it manages. Transactions must be recorded immediately after they are entered into in accordance with the principles of orderly book-keeping. There are no disclosure obligations concerning non-arms-length transactions. However, these transactions are allowed at market prices only, and best execution should be ensured. Securities lending activities are regulated in detail by the SFBC, may be carried out through banks, brokers, insurance companies or securities clearing organizations, and must always be settled through the custodian bank. The fund management company normally does not register the name of the unit holders, and the units are issued in bearer form. However, those in charge of marketing units issued by investment funds are obliged to fulfill the legislation on anti-money laundering and to identify the customer. The SFBC may withdraw the authorization if the fund does not comply with the relevant regulatory provisions. It may issue orders to correct irregularities and may appoint an observer (in the case the company is unable to fulfill its duties). Within one year, the observer must report to the SFBC. The supervision model for investment funds follows the same approach as for banks and securities dealers. External auditing firms examine compliance with the regulatory standards. They also examine whether the authorization requirements are fulfilled. Once the fund management company has been authorized, the auditing firm must verify compliance with the relevant legislation as well as with the Code of Conduct (including areas where conflict of interest may

	arise). There is no maximum term for the auditors. Breaches or irregularities must be notified to the SFBC, which, if necessary, will take further actions. The fund management company must, in any case, notify the SFBC of changes in (i) members of the board of directors or those who are responsible for managing the company; and (ii) persons possessing directly or indirectly at least 10 percent of the capital or voting rights or who can influence directly or indirectly the business activities of the fund (including persons acting in concert).
Assessment	Implemented.
Comments	Comments on the delegation of front-line supervisory responsibilities to external auditor apply (Principles 8, 9 and 10). In the case of collective investment schemes, however, the custodian bank, as an additional entity, has to verify that the fund managers behave correctly in the interest of investors. However, normally the custodian belongs to the same group as the fund management company. Improvements could be introduced in the area of disclosure of transactions that are not arms-length.
Principle 18.	The regulatory system should provide for rules governing the legal form and structure of collective investment schemes and the segregation and protection of client assets.
Description	According to the law, the management company must be a limited company with its registered office and principal place of administration in Switzerland. The fund must be created as a contractual fund (i.e., unit trust type). As far as foreign funds are concerned, the definition is broader and includes any type of pool of assets or SICAV-type funds (money market funds). The assets of a fund have to be segregated and they must be entrusted to a separate entity (the custodian bank). It is the responsibility of the custodian bank to ensure proper segregation. The custodian must be a licensed Switzerland-based bank. It is required to appoint a special officer responsible for discharging the custody function vis-à-vis the SFBC and the external auditors. In addition to ensuring the safekeeping of the fund's assets, the custodian bank must perform certain control functions, including verifying compliance with the fund's by-laws and other regulatory requirements, in particular in respect of investment decisions, calculation of the value of the units, and appropriation of income. The segregation principle is observed also in the case of bankruptcy procedures. Creditors of the management company do not have a claim on the fund's assets. In case of misbehavior of the asset management company or of the custodian, the SFBC may order to appoint a new custodian bank or to wind down the fund. It may also refer the case to the Federal Ministry of Finance or to the public prosecutor. Investors may sue the fund for compensation. The SFBC may ask that in case of class actions, unit holder representatives be allowed to participate in the procedure.
Assessment	Implemented.
Comments	
Principle 19.	Regulation should require disclosure, as set forth under the principles for issuers, which is necessary to evaluate the suitability of a collective investment scheme for a particular investor and the value of the investor's interest in the scheme.
Description	The law requires the fund management company to publish a prospectus for each fund that it manages. The prospectus must contain the fund rules and all other information required by the standards issued by the Swiss Funds Association and endorsed by the SFBC. The prospectus should highlight the nature of the fund and the instruments in which it can invest. Special requirements are applicable to risky funds such as hedge funds and derivative funds. The prospectus (and the subsequent amendments) must be submitted to the regulator. The SFBC does not approve the prospectus prior to its publication but can veto its publication. The SFBC

	may ask for the publication of additional information or amendments. The prospectus must be offered free of charge to the investor prior to entering into an agreement. The fund management company, for each fund it manages, is also required to publish annual as well as half-yearly reports. Advertising material is not subject to the same disclosure requirements as the offering materials (prospectus), but it has to refer to the offering material and indicate where the prospectus is available. Changes to the fund rules must be submitted to the SFBC for approval. If approval is granted, the investors are notified and they have the right to raise objections. If this is the case, the SFBC must refer the matter to the relevant judicial authority.
Assessment	Implemented.
Comments	
Principle 20.	Regulation should ensure that there is a proper and disclosed basis for asset valuation and the pricing and the redemption of units in a collective investment scheme.
Description	The Swiss Funds Association has issued "guidelines on the calculation of net asset values and the handling of valuations errors," which have been endorsed by the SFBC. According to Articles 48 par.1 and 49 par. 2 and 3 of the Investment Funds Act, the assets must be valued at their market value. To ensure uniform implementation of this requirement, the Swiss Funds Association has issued the above guidelines. If the shares are listed, market value refers to the last price paid. The assets are marked to market at the end of the accounting year and at the end of each day in which units are issued or redeemed. External auditors monitor net asset calculations. The price is disclosed whenever fund units have been issued and/or redeemed, at least twice a month in at least one daily or weekly newspaper. In practice, most funds calculate and publish their prices on a daily basis. Moreover, data are published on the SWX website (http://www.swx.ch). The SFBC, exceptionally and in the interest of investors, may suspend the redemption of fund units. Funds may stipulate rules covering special circumstances such as the closing of relevant markets, restrictions on foreign currency transactions, or extraordinary high volumes of redemptions. Although there is no prior approval requirement, the management company must communicate its decision without delay to the auditors, the SFBC, and the investors.
Assessment	Implemented.
Comments	
Principle 21.	Regulation should provide for minimum entry standards for market intermediaries.
Description	The law as supplemented by the implementing ordinance establishes the main criteria for authorization of securities dealers. According to the law, there are five categories of securities traders: (i) securities traders for their own account (with gross turnover that exceeds SwF 5 billion per year); (ii) issuing houses, which offer securities on the primary market; (iii) institutions dealing in derivatives, which issue and offer derivative products to the public on the primary market; (iv) market makers, which trade on their own account and quote prices to the public for certain securities; and (v) securities traders on behalf of the customer. To be included in the latter category, additional criteria have to be met. For example, the trading must be done on a "professional basis" (meaning that it is an independent economic activity directed at achieving regular revenues—which is presumed if the trader directly or indirectly maintains accounts or securities deposits for more than 20 customers). Entities subject to prudential supervision, shareholders or partners with a significant participation in the securities dealer's capital, and other institutional investors are not considered "customers." Therefore,

	securities dealers who provide services to these entities do not need to be authorized and supervised. The above-mentioned categories of securities dealers must obtain a license from the SFBC. The license—although by its nature universal—is granted for the proposed activity and category in order to meet the specific organizational set-up needed for that activity. Specifications on the activities carried out by the intermediary can be found in the by-laws. Amendments to the by-laws have to be submitted to the supervisory authority. Banks wishing to trade on securities markets must be licensed as securities dealers. A securities dealer license is always required to operate directly on stock exchanges (in Switzerland or abroad). Individual portfolio management is not considered as a regulated activity. It does not fall under any of the five above-mentioned categories and therefore no authorization from the SFBC is required. However, an asset manager must not maintain accounts or securities deposits in his or her name and on behalf of customers. Asset managers are only subject to anti-money laundering legislation and supervision. Licensing requirements are established in the law as supplemented by the relevant implementing ordinances and circulars. The SFBC may authorize as securities dealers individuals, partnerships, or corporations. A license is granted to the firm as such; employees are not individually licensed. However, during the licensing process, the SFBC assesses the fitness and propriety of senior management. Personnel authorized to trade on stock exchanges must fulfill the professional requirements contained in the rules of the exchanges. In case of corporations, the SFBC also assesses the propriety of major shareholders (above 10 percent of capital) and changes in major shareholding have to be notified to the SFBC. The securities dealer must demonstrate to possess an internal organization that ensures proper management. There is no deadline for the licensing process in the securities law. However, the general law on administrative procedures provides for a 90-day deadline. For the purpose of verifying the applicant's information, the SFBC does not carry out direct investigations, and relies on a detailed report by an external auditor. In practice, the formal licensing process (i.e., submission of a formal request) is normally preceded by an informal consultation between the applicant and the SFBC in order to ensure a smooth processing of the request. If the applicant fulfills the criteria spelled out in the legislation, the license is granted. The SFBC has the power to suspend or revoke the license and to impose remedial action on the intermediary. Denial of a license is subject to an appeal to the Swiss Federal Court. The SFBC publishes the list of authorized intermediaries on its website (http://www.ebk.admin.ch).
Assessment	Partially implemented.
Comments	Earlier comments on the lack of prudential regulation for asset managers (see Principle 1) and on the role of the external auditors are relevant (see Principles 8, 9 and 10). There seems to be a regulatory gap for dealers who trade on their own account (below the threshold of SwF 5 billion) or dealers who provide services to qualified professional investors only. According to the SFBC, these dealers do not constitute a threat for the stability of the system and do not raise investor protection concerns. Therefore, they do not warrant prudential regulation. However, these dealers must be authorized to trade directly on the SWX or on any other exchange. As mentioned earlier, an expert commission is currently drafting legislation for prudential oversight for asset managers and investment advisors.
Principle 22.	There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries undertake.
Description	All supervised intermediaries are required to possess a minimum initial capital. It is a flat amount applicable to all securities dealers and has to be paid in full. If the dealer is not incorporated or it is a partnership, the initial capital can be replaced by a guarantee on the private account of the dealer or partner (in this case a declaration by the owners of the account stating that their claims

	will be subordinated, is necessary). The SFBC may also authorize the intermediary to deposit collateral up to the amount of the required initial capital. Detailed requirements are provided for capital. The SFBC takes into account credit and market risk (mirroring requirements in the banking area). The SFBC has some discretion in modifying capital requirements in individual cases. Monitoring is carried out by external auditors. The securities dealers have to report to the SNB on a quarterly basis and have to provide consolidated semi-annual reports. External auditors are obliged to report as soon as losses reduce the capital by 50 percent. The SFBC may demand remedial measures from the firm concerned and can order the closure of the intermediary and its liquidation.
Assessment	Implemented.
Comments	
Principle 23.	Market intermediaries should be required to comply with standards for internal organization and operational conduct that aim to protect the interests of clients, ensure proper management of risk, and under which management of the intermediary accepts primary responsibility for these matters.
Description	Swiss regulation contains requirements on internal organization and Chinese walls. Measures to prevent conflict of interest and to ensure a proper management of conflict have to be in place. An internal audit function is required. However, small firms may outsource this function (normally to the internal auditor of the parent company). Record keeping and separation between customer assets and firm assets are required. The anti-money laundering law stipulates rules on the identification of the customer and, if required, the beneficial owner (see the assessment of anti-money laundering practices). It seems to be common practice to tape phone conversations between traders and customers. A written contract with the client is the normal practice. However, it is not mandated by law. Guidelines of the SBA require a written contract in the case of asset management, which, however, is not included under securities activities according to categories set out by SESTA (see Principle 23 above). The securities dealer must implement conduct of business rules, including, according to the law, a duty to provide information to the customer, a duty of care, and a duty of "loyalty." The business experience and the specialized knowledge of the customer should be taken into account. The principles established by the law have been supplemented by the SBA rulebook. This Code has been endorsed by the SFBC and has become mandatory for all securities dealers. The comparison with the conduct of business principles listed in the IOSCO Principles shows that certain areas such as the obligation to ask customers for information on their financial situation and the investment objectives are not covered by the Swiss conduct of business rules. There are no special requirements concerning customer suitability tests. The risk profile of the customer seems to be analyzed only when the intermediary provides additional individual investment advice. There are no rules concerning the obligation to disclose conflict of interest situations (the code of conduct rule book provides only for an ex post disclosure). In the case of risky products, a risk disclosure statement must be offered to the client. The risk disclosure statement is drafted according to standard models. Furthermore, normally securities dealers use standard forms where the customer acknowledges that he/she is aware of the risks involved in the transactions. The conduct of business rules must be applied also in the case of online provision of services. There are no particular rules applicable to proprietary trading activities under securities dealer regulations. Electronic trading systems could be regulated by the SFBC as organizations similar to exchanges.
Assessment	Partially implemented.
Comments	Conduct of business rules could be supplemented by SFBC instructions to ensure a higher degree

	of investor protection (especially in the area of suitability tests and the disclosure of conflict of interest). The conduct of business rules could also include rules aimed at ensuring market integrity. Rules concerning the identification of clients and beneficial owners are discussed in the anti-money laundering assessment.
Principle 24.	There should be a procedure for dealing with the failure of a market intermediary in order to minimize damage and loss to investors and to contain systemic risk.
Description	The SFBC may order an intermediary to take remedial actions; it may appoint an observer, or order the transfer of client assets to another intermediary. Winding down procedures for supervised institutions are regulated, except for few exceptional rules, by general bankruptcy law. The SFBC may order the liquidation of an institution, can withdraw its license and prohibit the making and receiving of payments. The SFBC, however, does not have the power to issue orders to protect the institution and insulate it from creditor actions. This power belongs to the cantonal courts. Winding down procedures involving international groups may involve coordination with responsible foreign regulators. However, the recognition of insolvency measures imposed by the foreign regulator will be decided by the relevant courts.
Assessment	Implemented.
Comments	A new draft bill is under consideration that would introduce more specific rules for regulating the failures of financial intermediaries (banks, securities dealers).
Principle 25.	The establishment of trading systems including securities exchanges should be subject to regulatory authorization and oversight.
Description	An exchange, according to Swiss law, is an organization which is set up for the purpose of securities trading and which enables the simultaneous exchange of offers of securities among a number of securities dealers, as well as the execution of transactions. The SFBC is responsible for licensing exchanges or for granting exemptions from the obligation to register as an exchange when certain criteria are met. It is up to the Federal Council to define such criteria. Exempted trading systems are not subject to prudential supervision. There is an ongoing debate within the SFBC about the type of treatment to be accorded to electronic communication networks (ECNs). A decision whether to grant ECNs an authorization as securities dealers or as organized trading markets has not been taken. So far, the SFBC has authorized as exchange the SWX Swiss Exchange and Eurex Zürich AG (which both act as SROs). An exemption from the obligation to register as an exchange has been granted by the SFBC to the International Securities Markets Association (ISMA), which has been authorized as an "institution similar to a stock exchange." The SWX operates different market segments, including small caps and fast growing equities (New Market); investment funds; corporate and government bonds, including Eurobonds and warrants. Since the second quarter of 2001, the SWX is part of a joint venture operating the UK-regulated market Virt-X. As a result, the trading of Swiss blue chips (SMI segment) takes place exclusively on Virt-X. The SWX has maintained its responsibilities as a listing authority. Securities dealers admitted to trading on the SWX are automatically admitted to trade on Virt-X. Eurex, which is a 50-50 joint venture between the SWX Group and Deutsche Börse, is one of the largest derivatives markets in the world. The SFBC is responsible for the authorization of Eurex Zürich AG. Special arrangements are in place for the supervision of Eurex. There is continuous cooperation between the Swiss and the German market surveillance departments. In addition, the Eurex Zürich surveillance team and the SWX team cooperate within the same surveillance office in Zurich. Notwithstanding this close cooperation, exchange of confidential information must take place according to relevant rules on administrative assistance. To be licensed, an exchange must demonstrate that its rules and internal organization are appropriate for fulfilling its tasks. The managers responsible of the exchange are subject to a fit

	and proper test. Minimum capital requirements are not a condition for authorization. The exchange must submit its rules and any subsequent amendment to the SFBC for approval. The rules can be approved only if they guarantee transparency and equal treatment of investors, and ensure a smooth functioning of the exchange. There is no obligation to subject the owner of the system to a fit and proper test (such as for securities dealers and fund management companies). However, the SFBC interprets its mandate such that it is allowed to inquire about the ownership of an exchange (even if this is not formally provided for by law). Once authorized, an exchange is responsible for supervising compliance with its own rules. The stock exchange can admit members to trading only if they are licensed by the SFBC as securities dealers. The exchange notifies the SFBC in cases when it receives requests from foreign securities dealers. Foreign dealers may be admitted to trading on Swiss exchanges only if the responsible foreign regulator confirms to the SFBC that they do not object, that the foreign dealers are properly supervised, and that the foreign regulator is in a position to offer administrative assistance. The SWX distinguishes between members and participants. The members are also the associates and must be Swiss securities dealers. Participants, which include the members, are all dealers that are admitted to trade on the trading platform (including remote members). The exchange, in order to be authorized, must maintain separate functions for admission to listing and supervision (see Principles 7 and 8). Channeling of orders via order routing systems installed with third parties is possible only with the prior agreement of the SWX. The authorized exchange is responsible for maintaining relevant audit trails of all transactions carried out on its trading platform. Over-the-counter (OTC) transactions in listed securities must be reported to the SWX. According to its rules, the SWX may ask participants for information deemed necessary for its investigations, and it may require the auditors of the participant to verify compliance with SWX rules. However, the SWX is unable to ask for the name of the beneficial owner of a transaction carried out on its system. The SFBC can ask the intermediaries to provide that information without restriction, however the SFBC can communicate this information to foreign supervisory authorities only if the client agrees. If the client does not agree, a judicial procedure may be initiated (see Principles 10 and 11). Moreover, there are restrictions on the permissible use of information (see above).
Assessment	Implemented.
Comments	As far as the supervision of the exchanges is concerned, remarks on the use of external auditors (see Principles 7 to 10) apply. However, the SFBC can exercise direct supervisory functions whenever deemed necessary to enforce the Securities Act. Comments made earlier on the exchange of information under Principles 11 to 13 apply.
Principle 26.	There should be ongoing regulatory supervision of exchanges and trading systems, which should aim to ensure that the integrity of trading is maintained through fair and equitable rules that strike an appropriate balance between the demands of different market participants.
Description	The SFBC does not monitor a securities exchange directly. The authorized exchange must appoint an external auditor (chosen among those recognized for auditing securities dealers). The auditor must verify annually whether the stock exchange has fulfilled the relevant regulations. Every year, the auditor must submit a report to the Board of Directors, the surveillance department, and the SFBC. The SFBC may withdraw authorization of an exchange that no longer fulfills the authorization requirements, or has serious breached the rules. Before withdrawing the authorization, the SFBC may order the exchange to undertake remedial actions. The SWX is a fully electronic order-driven trading system. Orders are matched based on price-time-priority criteria. According to SWX rules, all traders are granted an equal treatment: all of them have the same access to the system; data transmitted by the system are available to all

	participants simultaneously; participants' entries are processed according to entry timing; pricing is made in accordance with the same SWX matching rules. In the main market segment, participants are free to act as market makers if they wish. In the New Market segment (small caps), the presence of a market maker for each listed security is mandatory, and it is a pre-condition for the listing.
Assessment	Implemented.
Comments	Earlier comments on external auditors discussed under Principles 8 to 11 apply.
Principle 27.	Regulation should promote transparency of trading.
Description	The Law on Exchanges and Securities Trading requires an authorized exchange to ensure proper transparency of trading. According to SWX rules, the following data must be published: prices, volumes and timing; best bid and ask prices (with the relevant quantities); and total volumes and data related to reported off-exchange transactions. The public must also be informed when relevant interventions (such as non-opening, interruption, and suspension of trading) have occurred. Market traders are entitled to receive, on a continuous basis, the following information: all bid and ask prices with the correspondent quantities, all reported off-exchange transactions, and all indications of interests.
Assessment	Implemented.
Comments	
Principle 28.	Regulation should be designed to detect and deter manipulation and other unfair trading practices.
Description	Swiss law, including criminal law, prohibits market manipulation and other unfair trading practices. Responsibility for prosecution lies with competent criminal authorities. Guidelines of the SBA forbid certain practices such as front running. The SFBC is working on a circular on conduct of business rules for market integrity. The exchange/SRO must ensure continuous market monitoring. The Supervisory Department of the exchange reports relevant findings and ongoing investigations to the SFBC. The Supervisory Department may ask the participants' auditors to investigate on its behalf. In case of non-compliance or irregularities by a participant, the exchange/SRO may impose limitations on future trading, revoke trading privileges, and suspend the participant from trading. The court of arbitration settles disputes between participants and SWX, and disputes among participants arising from participation. Where appropriate, the internal remedies available at SWX (Disciplinary Commission, Appeals Board) shall be exhausted before regress can be sought at the court of arbitration.
Assessment	Implemented.
Comments	The principle can be implemented at national level. However, limitation on the ability of the SFBC to exchange information about clients could affect proper supervision of other markets. See Principles 11 to 13 for remarks about international cooperation.
Principle 29.	Regulation should aim to ensure the proper management of large exposures, default risk and market disruption.
Description	There are no specific rules for the supervision of large exposures of market participants and their clients. In particular, the exchange/SRO is not entitled to ask for the name of the customers. The rules of the exchange must include procedures for dealing with emergency situations and spell out default procedures. In cases of emergency, the SWX may take the necessary measures, including delaying the opening of trading in a given security, interrupting or suspending trading, as well as delisting

	securities. It may also decide to suspend rules or regulations in whole or in part, temporarily replace them, or suspend trading altogether. In the event of system failure, the SWX is responsible for providing mechanisms to continue trading until normal conditions are restored. Procedures for the deletion of orders in emergency situations are available. In special cases, participants must issue settlement instructions directly to the clearing organization. Similar provisions are applicable to Eurex. Market participants must join the market solidarity fund (i.e. the fund that covers monetary losses resulting from unfulfilled or only partially fulfilled obligations arising from transactions carried out on the market). In addition, each SWX participant must provide a collateral deposit of at least SwF 500,000 at SegaInterSettle AG (SIS). This collateral covers compensation for possible monetary damages and serves as a guarantee for fines imposed by the exchange.
Assessment	Implemented.
Comments	
Principle 30.	Systems for clearing and settlement of securities transactions should be subject to regulatory oversight, and designed to ensure that they are fair, effective and efficient and that they reduce systemic risk.
Description	Trades on SWX are settled via SIS. SIS also acts as a central security depository (CSD) and as an international CSD (ICSD). SIS has been authorized as a bank, and there are no special rules for the licensing of the settlement system. Eurex Clearing House is supervised as part of the exchange authorization process. German competent authorities supervise all other aspects related to Eurex Clearing. SIS is a wholly owned subsidiary of the Swiss Financial Services Group (53 percent is owned by Credit Suisse and UBS). It is supervised by the SFBC as a bank. SIS also provides a trade matching service; exchange matched transactions are communicated to SIS and settled by SIS as "locked in trades." OTC transactions of SIS participants can be matched and settled in the SECOM system of SIS. The SWX settles trades on a T+3 basis. SIS provides for a simultaneous, final, irrevocable delivery-versus-payment real time gross settlement for Swiss franc transactions. Cross-border securities transactions are settled through custodians in the corresponding countries. In the Swiss system, securities lending transactions are not restricted. Short selling is permitted. Rules of conducts have to be fulfilled when client money or securities are involved. There are rules on the use of collateral in Swiss law. However, financial collateral is not fully insulated from insolvency procedures.
Assessment	Implemented.
Comments	Swiss regulations could be improved by providing for full insulation of financial collateral from insolvency procedures. Proposed new legislation on bank reorganization and liquidation would provide for the immediate enforcement of financial collateral in case of insolvency. Special rules on the licensing of clearing and settlement systems could also be introduced, since the business performed by entities such as SIS is not a typical banking business. Special requirements on capital adequacy, operation and supervision could strengthen the ability of the system to handle financial distress. Limit on cooperation with foreign supervisors may however affect proper supervision.

Based on the detailed assessment, a *summary* table of assessment of observance is presented in Table 5.

Table 5. Summary Observance of the IOSCO Objectives and Principles

Assessment Grade	Principles Grouped by Assessment Grade	
	Count	List
Implemented	17	4, 5, 6, 7, 8, 17, 18, 19, 20, 22, 24, 25, 26, 27, 28, 29, 30
Partially Implemented	13	1, 2, 3, 9, 10, 11, 12, 13, 14, 15, 16, 21, 23
Non-Implemented		
Not applicable		

Recommended action plan and authorities' response to the assessment

Table 6. Recommended Action Plan—IOSCO Objectives and Principles

Reference Principle	Recommended Action
Principles 1-5. Relating to the Regulator	Securities regulation should be updated to include all types of securities transactions and securities intermediaries, including primary markets and all asset managers. Modalities for removal of board members could be clearly spelled out in the law. Rules on incompatibilities with other professional activities could be improved. Full budgetary independence should be granted to the SFBC, and an increase in its staff resources would be justified.
Principles 6-7. Self-Regulation	A more proactive role for the SFBC in supervising SROs is desirable. The role performed by certain trade associations in regulation and supervision could be formalized.
Principles 8-10. Enforcement of Securities Regulation	Enforcement powers of the SFBC could be strengthened. In particular, it would be desirable to increase direct supervision, formalize the examination process and quality assurance for external auditors, and increase the range of available sanctions.
Principles 11-13. Cooperation in Regulation	Efforts by the SFBC to strengthen cooperation with foreign regulators are recommended.
Principles 14-16. Issuers	There is room to improve protection for minority shareholders and strengthen accounting and auditing regulations to ensure comparability of financial information. It would also be advisable to introduce proper supervision and sanctioning of auditors of listed companies.
Principles 17-20. Collective Investment Schemes	Improvements are possible in the area of asset valuation, where a more direct involvement of the regulator could be envisaged.
Principles 21-24. Market Intermediaries	Supervision of market intermediaries could be strengthened by supervising dealers that trade on their own account but whose business volume falls below the official threshold, and those that provide services only to qualified professional investors. Rules on disclosure of conflict of interest before conducting the transaction could be provided.
Principles 25-30. Secondary Market	The supervisory role of the SFBC with regard to secondary markets could be strengthened. Proper supervision of international exchanges requires full ability to provide information; see recommendation under Principles 11 to 13.

Authorities' response

In general, the authorities agreed with the key findings and with most of the recommendations. They agreed that budgetary independence of the SFBC could be strengthened, but viewed full prudential regulation of asset managers and investment advisors who do not manage funds in their name on behalf of clients, and small firms that trade on their own account, as unnecessary. They supported the recommendation for additional sanction powers as useful but not strictly necessary. The SFBC noted that in its view, prudential supervision of firms who trade on their own account below the threshold of SwF 5 billion is not required from the perspective of investor protection nor from that of financial system stability. On the need for a more proactive role in supervising SROs and primary and secondary markets, the authorities noted that the SFBC in most cases has the authority, if needed, to directly supervise SROs, securities dealers, and markets. They did not consider direct responsibility of the SFBC with respect to accounting and auditing standards as necessary, since the SFBC's approval of SWX listing rules, which prescribe acceptable accounting and auditing standards, provides the regulator with indirect competence in this area.

III. IAIS INSURANCE CORE PRINCIPLES

The assessment of the Swiss Insurance Sector was performed as part of the Financial Sector Assessment Program (FSAP) for Switzerland.[6] The main objectives of the assessment were to determine the levels of observance with the International Association of Insurance Supervisors (IAIS) principles, and to suggest areas where further development is appropriate.

The assessment was based on a review of the legal framework, and extensive discussions with the supervisory authorities and market participants. It focused mainly on the supervisory work of the Federal Office of Private Insurance (FOPI) under the Ministry of Justice and Police.

The supervisory staff of the FOPI cooperated extensively in the assessment by providing answers to a questionnaire, preparing a self-assessment against IAIS Core Principles, and making themselves available to meet with mission members.

Information and methodology used for assessment

The assessment is based on legislation applying to the insurance sector. The following laws apply:

961.01 (June 23, 1978)	Supervision of private insurance companies (Versicherungsaufsichtsgesetz)
961.02 (February 4, 1919)	Guarantees for operations carried out by foreign insurance companies (Kautionsgesetz)
961.03 (June 25, 1930)	Securing life insurance claims (Sicherstellungsgesetz)
961.61 (June 18, 1993)	Direct life insurance (Lebensversicherungsgesetz)
961.71 (March 20, 1992)	Direct non-life insurance (Schadenversicherungsgesetz)
221.229.1 (April 2, 1908)	Insurance contracts

In addition to these laws, there are the following ordinances and decrees:

955.032 (December 14, 1999)	Anti-money laundering
961.011 (November 1978)	Implementation of the law on supervision of private insurance companies
961.015 (November 1997)	Investments in derivatives
961.05 (September 11, 1931)	Supervision of private insurance companies
961.11 (February 11, 1976)	Scope of insurance supervision

[6] The assessment was prepared by Donald McIsaac, lead insurance specialist, Financial Sector Department of the World Bank and Johan Altersten, supervision process manager, Finansinspektionen of Sweden. The assessment is based on information available during the FSAP mission in October 2001.

961.13 (December 3, 1979)	Non-insurance business performed by private insurance companies
961.21 (November 19,1955)	Sellers and buyers insurance
961.22 (November 18, 1992)	Legal aid insurance
961.27 (November 18, 1992)	Damages from natural causes
961.611 (November 29, 1993)	Direct life insurance
961.711 (September 8, 1993)	Direct non-life insurance
961.795 (November 18, 1992)	Equalization reserve in credit insurance
221.229.11 (March 1, 1966)	Removing certain restrictions on the formation of insurance contracts
281.51 (May 10, 1910)	Seizure, sequestering and realization of proceeds from insurance claims
741.31 (November 20, 1959)	Decree on motor third party liability insurance

The assessment was performed using the Core Principles Methodology report adopted by the IAIS at its meeting in October 2000. The IAIS has developed 17 principles for effective insurance regulation and supervision. A principle will be considered **observed** whenever all essential criteria are generally met without any significant deficiencies. A principle will be considered **broadly observed** whenever only minor shortcomings are observed, which do not raise any concerns about the authority's ability and intent to achieve full observance with the principle within a prescribed period of time. A principle will be considered **partly observed** whenever, despite progress, the shortcomings are sufficient to raise doubts about the authority's ability to achieve observance. A principle will be considered **non-observed** whenever no substantive progress toward observance has been achieved. A Principle will be considered **not applicable** whenever the CP does not apply given the structural, legal and institutional features of a jurisdiction.

Institutional and macroprudential setting—overview

The insurance sector in Switzerland is very concentrated. The largest ten insurance companies cover about 90 percent of the insurance market. The Swiss insurance industry has significant interests abroad. Most cross-border operations are in the form of subsidiaries to Swiss insurance companies. Several foreign insurance companies carry out business in Switzerland. The Swiss insurance industry is highly developed. Insurance purchases by residents of Switzerland ranks among the highest rates of such consumption in the world. Swiss companies have not confined themselves to operations in Switzerland and some of them rank among the big suppliers of insurance throughout Europe—either directly or through subsidiary members of a number of conglomerate groups. For some of these organizations, fully one-half of their premiums come from outside Switzerland.

The following tables provide statistics that are widely quoted as indicative of the development of an insurance market. The first table provides information on insurance premiums per capita for the year 2000 (in U.S. dollars), often referred to as "premium density":

	Total business	Non-life business	Life business
Switzerland	4,154	1,571	2,583
Japan	3,973	808	3,165
United Kingdom	3,759	730	3,029
United States	3,152	1,541	1,611
Ireland	2,552	664	1,888
Netherlands	2,290	933	1,357

Source: SIGMA/Swiss Re, *World Insurance in 2000*. Social security contributions are excluded.

Another widely quoted statistic is the ratio of premiums to Gross Domestic Product, referred to as the rate of insurance penetration. The following table shows the 2000 statistics for the five countries with the highest percentage ratios:

	Total business	Non-life business	Life business
South Africa	16.86	2.83	14.04
United Kingdom	15.78	3.07	12.71
South Korea	13.05	3.16	9.89
Switzerland	12.42	4.70	7.72
Japan	10.92	2.22	8.70

Source: SIGMA/Swiss Re, *World Insurance in 2000*.

As the tables indicate, Swiss residents are among the world leaders in the purchase of insurance.

The insurance market in Switzerland is highly concentrated even though there are a large number of companies. The following table provides information on the number of players in the market.

	Life	Non-life	Reinsurance	Total
Domestic	28	73	35	136
Foreign	2	35	-	37
Total	30	108	35	173

Of the 30 life companies operating in the Swiss market, only five companies received over 75 percent of total premiums paid for life insurance business in the year 2000. In the non-life business, 10 companies collected over 75 percent of premiums paid for non-life insurance in

Switzerland during the year 2000. This leaves a relatively small amount of premiums to be divided up among the many other licensed companies.

Management of Swiss insurance companies share the belief that there remains little opportunity for growth in the domestic insurance market. In the area of non-life insurance, they speak of a "saturated" market. Growth potential in the life insurance area is also regarded as limited although there may still be some opportunities for growth from the pension business. With this picture in mind, companies have been exploring the opportunities for selling policies in other countries and have been expanding their operations through acquisition in other countries. The United States was regarded by some as an area with potential for growth.

General preconditions for effective insurance supervision

In order to carry on insurance activities in Switzerland, a company must be licensed by the Ministry of Justice and Police. The FOPI is responsible for supervision of the private insurance market.

Swiss legislation is not very specific on obligations and powers of the supervisory authority. In some ways, this gives quite extended supervisory powers to the Minister of Justice and Police, who is formally responsible for decisions in this area. In practice, however, decision-making in general is delegated to the FOPI's Managing Board. This implies that the range and quality of supervision to a large extent depends on the composition of the Board.

The FOPI has its own annual budget, approved by the Ministry of Justice and Police. The costs for supervision are charged to the insurance companies afterwards. For that purpose, the FOPI prepares an annual record of the cost of its operations. The contributions are paid directly to the Treasury, and the FOPI may not keep any eventual "surplus."

Of a total staff of 55, the professional members of the FOPI dedicated to supervision number about 35—which is low by almost any standard, but in particular in light of the large size of the insurance industry in Switzerland. The FOPI is anxious to increase this number in order to augment its supervisory capacity. If it had more professional staff it could engage, for example, in more on-site inspections; strengthen offsite monitoring (including, e.g., in-depth analyses of the impact of recent asset market volatility on the insurance industry); intensify contacts with supervised companies; and strengthen cooperation with other supervisory agencies, both domestically and abroad. Steps in all these directions are recommended. Lack of flexibility with regard to salary scales has so far hampered recruitment efforts.

There are some shortcomings in the present supervisory model. One is in the area of changes in control of management or ownership. The FOPI does not give its approval of changes in ownership or carry out fit and proper assessments of major owners or management, since the present legislation does not give the authority those powers.

A critical feature to be submitted with an application for license is the "Business Plan." This document contains a description of the manner in which the company intends to conduct its

business and fixes the parameters of the pricing for insurance contracts, the computation for the technical provisions in support of those contracts, and the reinsurance treaty arrangements that the company will, or has, negotiated. The important feature is that this plan remains in force for as long as the company is licensed and the company will be expected to seek approval of the authorities for any amendment to the plan, even in such matters as changes to the parameters used to set premium rates for life and health insurance.

Another area of concern is insurance intermediaries. There is presently no legislation in Switzerland that applies to insurance brokers, nor is there a code of conduct regarding sale of insurance products by tied agents or others. This is an area of concern, since market conduct and consumer protection issues in many ways relate to the conduct of insurance intermediaries.

A third issue of concern is the lack of requirements on internal control systems in insurance companies. Insurance legislation does not cover the duties of the Board of Directors or the General Manager in this area. The FOPI has no legal basis to establish appropriate rules and has not issued any guidance. The legislation that to some extent covers internal controls and management is the general corporation legislation. In addition, the insurance legislation does not give directions regarding corporate governance, which has proven in other countries to be a key aspect of sound management practices, in particular in large and internationally active financial institutions. Since the FOPI has not provided formal guidance, no standards have been set in this area (except from the general provisions in the corporate legislation).

A new draft Bill will shortly be submitted to the Parliament. It is expected to become effective in 2003 and its rapid adoption is highly recommended. The new law will encompass the areas that are now covered by the Acts mentioned above. It will also cover the areas of changes in control and ownership and insurance intermediaries. Under the new law, Swiss insurance legislation will, in essential areas, be in line with EU regulations. The Draft Bill also sets the foundations for the supervision of insurance activities of financial conglomerates.

Principle-by-principle assessment

Table 7. Detailed Assessment of Observance of the IAIS Insurance Core Principles

Principle 1.	**Organization of an Insurance Supervisor** The insurance supervisor of a jurisdiction must be organized so that it is able to accomplish its primary task, that is, to maintain efficient, fair, safe, and stable insurance markets for the benefit and protection of policyholders. It should, at any time, be able to carry out this task efficiently in accordance with the Insurance Core Principles. In particular, the insurance supervisor should: – Be operationally independent and accountable in the exercise of its functions and powers; – Have adequate powers, legal protection, and financial resources to perform its functions and exercise its powers; – Adopt a clear, transparent, and consistent regulatory and supervisory process; – Clearly define the responsibility for decision-making; and – Hire, train, and maintain sufficient staff with high professional standards who follow the appropriate standards of confidentiality.
Description	Insurance supervision in Switzerland is regulated under six different laws and a number of ordinances and decrees. A new Draft Bill will shortly be submitted to the Parliament, which will bring Switzerland's insurance legislation closer to EU standards. The FOPI is an authority under the Ministry of Justice and Police. Its budget is subject to approval by the Minister and while it assesses a levy on each licensed company, it receives its funding from the Government. The actual cost for supervision is recovered in the following year from the insurance companies. The Minister of Justice and Police is formally responsible for decisions with respect to granting and withdrawal of licenses. In practice, many of the decision powers have been delegated to the Head of the FOPI. Of a total staff of 55, the professional members of the FOPI dedicated to supervision number 35. The FOPI is anxious to increase this number in order to augment its supervisory capacity. If it had more professional staff it could engage in more on-site inspections and expand its offsite monitoring of key developments in the industry, for example. There is a fixed salary scale within the public administration. Any deviation from that scale must be approved by the Ministry of Finance beforehand. This lack of flexibility has hindered recruitment. At present it is possible to hire specialists or "experts" at higher rates of compensation provided prior approval is obtained. However it would be preferable if the general program of compensation recognized the special competencies required by all FOPI professional staff; The head of the FOPI, as is the case for all public servants, is appointed by the Government for a period of four years (as of January 1, 2002 for an indefinite term) and can be removed at any time, if serious reasons justify such a measure. FOPI employees are not personally responsible for the consequences of operations by the FOPI, and they are shielded from any legal action with reference to the FOPI.
Assessment	Broadly observed.
Comments	The existing legislation is not very specific regarding the powers of the supervisor. In practice, the head of the FOPI exercises extensive control over the industry relying upon sections of the legislation that define in only the broadest terms the authority of the supervisor. It is not evident that a court will always support the actions of the supervisor if they are challenged. Quality and consistency in supervision depend to a large extent on the integrity and competence of the person who is heading the authority. The proposed new legislation is expected to make these powers more specific.

	The fixed salary scale on a public servant level may be a hindrance for recruiting and keeping highly skilled experts.
Principle 2.	**Licensing** Companies wishing to underwrite insurance in the domestic insurance market should be licensed. Where the insurance supervisor has authority to grant a license, the insurance supervisor: – In granting a license, should assess the suitability of owners, directors, and/or senior management, and the soundness of the business plan, which could include pro forma financial statements, a capital plan, and projected solvency margins; and – In permitting access to the domestic market, may choose to rely on the work carried out by an insurance supervisor in another jurisdiction if the prudential rules of the two jurisdictions are broadly equivalent.
Description	Switzerland is completely open for establishment of domestic and foreign insurance operations. All insurance companies must be licensed by the Ministry of Justice and Police. However the Ministry will only issue or withdraw a license on the recommendation of the head of the FOPI. The authority requires all appropriate forecasts and Business Plans when considering an application. The only weakness appears to be with regard to assessments of fitness and propriety. The present law does not contain specific provisions relating to the assessment of owners and managers. A critical feature to be submitted with an application for license is the "Business Plan." This document is a description of the manner in which the company intends to conduct its business. It also shows how the company plans to fix the parameters of the pricing for insurance contracts and to establish the computation for the technical provisions in support of those contracts. The document further establishes how the company will, or already has negotiated its reinsurance treaty arrangements. The important feature is that this plan remains in force for as long as the company is licensed, and any amendment to the plan will require approval of the authorities, even in such matters as changes to the parameters used to set premium rates for life and health insurance. Ordinances issued under the authority of the legislation specify minimum amounts of capital to be established by all applicants for licensing. The requirements vary according to the nature of business the company wishes to transact. Newly incorporated companies must also establish a special organization fund to which they can charge organizational expenses. All foreign insurance entities that seek to do business in Switzerland must be licensed and are subject to supervision by the FOPI. Unlike the situation for domestic companies, the FOPI will assess the fitness of management before licensing branches of foreign insurance companies**.** A special agreement has been negotiated with the European Union with respect to non-life insurance companies. This agreement permits the sharing of certain information between the FOPI and EU supervisors when they receive an application from an insurance company based in an EU member state. Otherwise, there is no reliance on the work of insurance supervisors in other jurisdictions.
Assessment	Broadly observed.
Comments	Fit and proper assessments are essential for the licensing process, However, at present they are not carried out for domestic companies in Switzerland, although there is a specific law relating to licensing of foreign companies that requires an assessment of whether local managers are judged to be fit and proper.

Principle 3.	**Changes in Control** The insurance supervisor should review changes in the control of companies that are licensed in the jurisdiction. The insurance supervisor should establish clear requirements to be met when a change in control occurs. These may be the same as, or similar to, the requirements which apply in granting a license. In particular, the insurance supervisor should: – Require the purchaser or the licensed insurance company to provide notification of the change in control and/or seek approval of the proposed change; and – Establish criteria to assess the appropriateness of the change, which could include the assessment of the suitability of the new owners as well as any new directors and senior managers, and the soundness of any new business plan.
Description	Changes in control of companies licensed in the jurisdiction do not need to be approved. The FOPI does not carry out assessments of management or owners, since the present legislation does not support this. As a principle, changes in control should be subject to the same scrutiny as a new license. The supervisor should be empowered to prevent any transfer of control.
Assessment	Non-observed.
Comments	According to EU legislation, transfer of ownership may not occur without the consent of the supervisory authorities. In any review of such a transfer, supervisors should carry out fit and proper assessments of management and major owners. This includes such items as competence, records of criminal activities, fiscal records, and records of any bankruptcies. According to the action plan for the FOPI, the new legislation, expected to be enacted in 2003, will provide the necessary authority to exercise control. Criteria will be established and increases in staff resources as well as out-sourcing of certain duties to private sector experts, will be sought.
Principle 4.	**Corporate Governance** It is desirable that standards be established in the jurisdictions which deal with corporate governance. Where the insurance supervisor has responsibility for setting requirements for corporate governance, the insurance supervisor should set requirements with respect to: – The roles and responsibilities of the board of directors; – Reliance on other supervisors for companies licensed in another jurisdiction; and – The distinction between the standards to be met by companies incorporated in his jurisdiction and branch operations of companies incorporated in another jurisdiction.
Description	Standards of Corporate Governance for insurance companies prevailing in Switzerland are those specified for all corporations through the corporate law. The insurance supervisor has no specific authorities in this area. Larger, well-managed companies have adopted international best practices for insurance company governance purposes. Since there are no guidelines imposed by the FOPI, it is uncertain as to the practices followed in smaller companies.
Assessment	Partly observed.
Comments	The insurance legislation does not give directions regarding corporate governance. Since the FOPI has not provided formal guidance, no standards have been set in this area (except from the general provisions in the corporate legislation). International best practices for insurance companies would suggest that there be special duties specified for Boards of Directors in areas such as setting investment policy, risk management policy and the establishment and monitoring of a system of internal controls.

Principle 5.	**Internal Controls** The insurance supervisor should be able to: – Review the internal controls that the board of directors and management approve and apply, and request strengthening of the controls where necessary; and – Require the board of directors to provide suitable prudential oversight, such as setting standards for underwriting risks and setting qualitative and quantitative standards for investment and liquidity management.
Description	The legislation does not provide the supervisor with specific authorities with respect to internal controls. The supervisor has no authority to require particular actions of Boards of Directors. Likewise, the supervisor has no authority to require oversight by the Board of Directors nor to require strengthening of the internal controls system. Supervisory staff reviews a company's system of internal controls during on-site inspection. Even without such specific powers, the FOPI could issue general guidelines indicating what is expected of companies in the area of internal controls. Internal controls are routinely reviewed by the external auditors and the larger companies appear to have developed extensive control systems. It is difficult to estimate the controls situations in smaller companies and how the management of these companies would be prepared to cope with stressful business conditions.
Assessment	Partly observed.
Comments	The insurance legislation does not provide directions regarding internal control. Since the FOPI has not issued any guidance, no standards have been set in this area (except from the general provisions in the corporate legislation). International best practices would suggest that the issue of formal guidelines in this respect would be an appropriate step for the supervisory authorities. According to the action plan for the FOPI, the new legislation, expected to be enacted in 2003, will provide the necessary authority to exercise control. Criteria will be established and increases in staff resources as well as out-sourcing of certain duties to private sector experts, will be sought.
Principle 6.	**Assets** Standards should be established with respect to the assets of companies licensed to operate in the jurisdiction. Where insurance supervisors have the authority to establish the standards, these should apply at least to an amount of assets equal to the total of the technical provisions, and should address: – Diversification by type; – Any limits, or restrictions, on the amount that may be held in financial instruments, property, and receivables; – The basis for valuing assets which are included in the financial reports; – The safekeeping of assets; – Appropriate matching of assets and liabilities; and – Liquidity.
Description	Companies must establish a pool of "tied assets" to cover the technical provisions in their non-life business and a "security fund" of a similar nature sufficient to cover the mathematical reserves in their life insurance business. These portfolios are monitored on a regular basis and the FOPI will ask the company to replace any asset within the supporting portfolio that has suffered a significant deterioration in value. Ordinances 961.611 (life insurance) and 961.711 (non-life insurance) give standards regarding the composition of the portfolios of assets covering technical provisions and mathematical reserves. The standards are compatible with EU-standards. The legislation specifies a "prudent management" approach to investment, calling for an investment program that respects the need

	for security, yield and diversification. The ordinance specifies that the following limits apply: - 30 percent of technical reserves may be invested in receivables towards counterparts in other countries. Receivables towards each counterpart may not exceed 5 percent. - 20 percent of technical reserves may be invested in receivables in foreign currencies. Receivables towards each counterpart may not exceed 5 percent. - 30 percent of technical reserves may be invested in Swiss securities and shares in Swiss companies. Receivables towards each counterpart must not exceed 10 percent. - 25 percent of technical reserves may be invested in foreign securities and shares in foreign companies. Receivables towards one counterpart must not exceed 5 percent. - 5 percent of technical reserves may be invested in foreign real estate. Investments with related parties must not exceed 5 percent of the portfolio. Auditors perform an annual review of the asset portfolio of each company to verify the identity, amount and valuation of the assets supporting technical provisions and mathematical reserves. Companies provide - monthly for life insurance and yearly for non-life insurance - statements showing changes in the amount and composition of investment portfolios.
Assessment	Observed.
Comments	Investment controls will be improved and greater risk management achieved once effective internal control procedures are in place. Close monitoring of developments in (the value of) assets of companies is required, in particular in times of asset market volatility.
Principle 7.	**Liabilities** Insurance supervisors should establish standards with respect to the liabilities of companies licensed to operate in their jurisdiction. In developing the standards, the insurance supervisor should consider: – What is to be included as a liability of the company, for example, claims incurred but not paid, claims incurred but not reported (IBNR), amounts owed to others, amounts owed that are in dispute, premiums received in advance, as well as the provision for policy liabilities or technical provisions that may be set by an actuary; – The standards for establishing policy liabilities or technical provisions; and – The amount of credit allowed to reduce liabilities for amounts recoverable under reinsurance arrangements with a given reinsurer, making provision for the ultimate collectability.
Description	Technical provisions for property and casualty business as well as mathematical reserves for the life insurance business must be computed using the methods and assumptions established in the company's Business Plan. Life reserves must be certified by a qualified actuary. Companies are expected to establish IBNR reserves and to compute this reserve using the method described in the Business Plan. The FOPI provides detailed instructions to companies regarding the computation and reporting of liabilities for various lines of business. Companies writing long-tail business must include a liquidation triangle or "run -off" table in their periodic reports to provide support for the adequacy of technical provisions. The credit for reinsurance is determined by the company. The FOPI reviews the strength and the claims-paying ability of reinsurance companies in the examination of the Business Plan. It also has authority to reject a reinsurer or to stipulate the amount of reinsurance credit that may be taken.
Assessment	Observed.
Comments	Life insurance companies play an important role in funding of the "second pillar" of the

	mandatory pension scheme. They are required to guarantee an interest rate not less than 4 percent per year on those funds. In light of the recent deterioration of investment performance, it appears unlikely that investment income of the funds will sustain this guarantee. If this rule is not amended, the insurance companies involved must be required to establish deficiency reserves.
Principle 8.	**Capital Adequacy and Solvency** The requirements regarding the capital to be maintained by companies which are licensed, or seeking a license, in the jurisdiction should be clearly defined and should address the minimum levels of capital or the levels of deposits that should be maintained. Capital adequacy requirements should reflect the size, complexity, and business risks of the company in the jurisdiction.
Description	Capital adequacy and solvency standards are given in ordinances 961.611 (life insurance) and 961.711 (non-life insurance). Most of the rules reflect EU regulations. <u>Non-life insurance</u> Minimum capital for insurance classes 1-8 and 10-15 is SwF 8-10 million Minimum capital for insurance classes 9 and 16 is SwF 3-7 million Minimum capital for insurance classes 17 and 18 is SwF 0.6-2 million <u>Life insurance</u> Minimum capital for life insurance is SwF 5-10 million The solvency margin is more relevant for established companies than are the minimum initial capital rules. Prescribed forms issued by the FOPI require companies to compute the required solvency margin using the EU formula and then to identify the admitted portion of "net worth" that is deemed to be applicable to cover the solvency requirements.
Assessment	Observed.
Comments	According to EU legislation, insurance companies that are part of an insurance group should be subject to solo-plus supervision, by which calculation of capital should take into account the impact of related companies upstream and downstream (in order to avoid double gearing). Supervisory focus for the FOPI is however on the individual entity. New draft legislation will go beyond what is required by EU-legislation and require consolidated supervision of insurance groups. Under special arrangements negotiated between the FOPI, the SFBC, and certain key financial conglomerates, these large Swiss companies are already under consolidated supervision.
Principle 9.	**Derivatives and "Off-Balance Sheet" Items** The insurance supervisor should be able to set requirements with respect to the use of financial instruments that may not form a part of the financial report of a company licensed in the jurisdiction. In setting these requirements, the insurance supervisor should address: – Restrictions in the use of derivatives and other off-balance sheet items; – Disclosure requirements for derivatives and other off-balance sheet items; and – The establishment of adequate internal controls and monitoring of derivative positions.
Description	There is a decree (961.015) regarding the use of derivatives, covering among other things internal controls with regard to handling of derivatives. According to the decree, insurance companies should have: - A strategy for use of derivatives, - Limits for risk exposure in derivatives, - A risk analysis system with regard to derivatives, and - An organization for internal controls for the use of derivatives. Internal controls should encompass:

	- Management and control, - Qualifications of persons involved, and - Reporting to management at least twice a year.
Assessment	Observed.
Comments	More than 40 of the licensed Swiss companies have made some use of derivative investment products in the past year. Close monitoring of developments in (the value of) derivative positions of companies is required.
Principle 10.	**Reinsurance** Insurance companies use reinsurance as a means of risk containment. The insurance supervisor must be able to review reinsurance arrangements, to assess the degree of reliance placed on these arrangements and to determine the appropriateness of such reliance. Insurance companies would be expected to assess the financial positions of their reinsurers in determining an appropriate level of exposure to them. The insurance supervisor should set requirements with respect to reinsurance contracts or reinsurance companies addressing: – The amount of the credit taken for reinsurance ceded. The amount of credit taken should reflect an assessment of the ultimate collectability of the reinsurance recoverable and may take into account the supervisory control over the reinsurer; and – The amount of reliance placed on the insurance supervisor of the reinsurance business of a company which is incorporated in another jurisdiction.
Description	As part of the Business Plan submitted with an application for licensing, insurance companies must outline their proposed reinsurance program. The details on the program Plan must be kept up-to-date thereafter and the changes provided to the FOPI. Insurance companies have to submit, on an annual basis, a list of the most important reinsurers and the volumes of business submitted to each such reinsurer. Further information about reinsurance programs may be collected at on-site inspections. There are no requirements regarding the maximum size of self-retention in relation to capital. However, there is a rule of thumb regarding minimum portfolio retention that is applied particularly to captives. There is no systematic procedure for the evaluation of the credit taken for reinsurance ceded, although the information contained in the Business Plan does provide the FOPI with an indication of the reinsurance companies to whom a company cedes business and this would permit as assessment of the claims-paying ability of the reinsurers. The FOPI requires companies to report specifically on the volumes of reinsurance that are ceded to related companies.
Assessment	Broadly observed.
Comments	Ceded reinsurance is of major importance in an insurance company, particularly for smaller companies. The quality of reinsurance also may have an impact on calculation of the solvency margin and some countries will ask for increased capital depending on the assessment of the claims-paying ability of the reinsurers. The amount of self-retention per risk and/or event in relation to capital may be crucial. Many countries have established a guideline that maximum retention on a single risk should not exceed 10 percent of capital.

Principle 11.	**Market Conduct** Insurance supervisors should ensure that insurers and intermediaries exercise the necessary knowledge, skills, and integrity in dealing with their customers. Insurers and intermediaries should: – at all times act honestly and in a straightforward manner; – act with due skill, care, and diligence in conducting their business activities; – conduct their business and organize their affairs with prudence; – pay due regard to the information needs of their customers and treat them fairly; – seek from their customers information which might reasonably be expected before giving advice or concluding a contract; – avoid conflicts of interest; – deal with their regulators in an open and cooperative way; – support a system of complaints handling, where applicable; and – organize and control their affairs effectively.
Description	Insurance agents are not required to be licensed but the FOPI relies on company management to train and monitor the behavior of their agents. Insurance brokers are not licensed under the present legislation, nor are they supervised by the FOPI. The FOPI has not issued any guidelines for the establishment of codes of conduct or of good business practice applying to either companies or intermediaries. When the FOPI receives complaints from policy holders, they contact the insurance company for further explanations. After analyzing the event, they give their view. The decision is, however, not legally binding. The FOPI does not require companies to establish a complaints-handling service. There is an insurance ombudsman, paid for by the insurance industry. In case of unresolved conflicts of interest, the policy holder may have to go to the court. The requirement of ethical codes should encompass the industry itself as well as all categories of intermediaries. It is not unusual that such codes are developed by trade organizations in cooperation with supervisors. The supervisor may want to issue general guidance on areas to be covered by ethical codes, for instance information to policy holders, treatment of customers, conflicts of interest, advice to customers etc., while the industry engages itself in more detailed guidelines relating to the specific lines of business in which it operates.
Assessment	Partly observed.
Comments	Tied agents—agents with exclusive ties with one insurance company—play an important role in selling insurance products. At the present, insurance brokers are mostly involved in selling commercial insurance products. It is, however, not unlikely that brokers will be more involved in the selling of products to consumers in the future. In relation to consumer protection, it is essential that all who are involved in selling insurance products comply with some kind of ethical code. The FOPI could issue guidelines regarding codes of conduct and also suggesting that companies establish claims resolution procedures.

Principle 12.	**Financial Reporting** It is important that insurance supervisors get the information they need to properly form an opinion on the financial strength of the operations of each insurance company in their jurisdiction. The information needed to carry out this review and analysis is obtained from the financial and statistical reports that are filed on a regular basis, supported by information obtained through special information requests, on-site inspections, and communication with actuaries and external auditors. A process should be established for: – setting the scope and frequency of reports requested and received from all companies licensed in the jurisdiction, including financial reports, statistical reports, actuarial reports, and other information; – setting the accounting requirements for the preparation of financial reports in the jurisdiction; – ensuring that external audits of insurance companies operating in the jurisdiction are acceptable; and – setting the standards for the establishment of technical provisions or policy and other liabilities to be included in the financial reports in the jurisdiction. In so doing, a distinction may be made: – between the standards that apply to reports and calculations prepared for disclosure to policyholders and investors, and those prepared for the insurance supervisor; and – between the financial reports and calculations prepared for companies incorporated in the jurisdiction, and branch operations of companies incorporated in another jurisdiction.
Description	Insurance companies submit detailed financial information on an annual basis. In addition, the FOPI receives a report once per year from the external auditors confirming the amount and proportional composition of the investment funds that support the technical provisions. FOPI has developed an analysis model called TEDAP. Reporting to the FOPI is done electronically. All data is fed into the TEDAP database, which can be used for various kinds of advanced analyses. Feedback is given on electronic media to the insurance companies. The FOPI has prescribed forms for annual reports and these conform to those prescribed for insurance companies by the EU. Accounting principles used by insurance companies in their consolidated statements to shareholders and the public follow a variety of accounting conventions depending on the scope of their operations and the markets in which their shares are traded. For example, companies might use US GAAP, Swiss GAAP, or IAS. Individual financial statements follow the provisions of Swiss Commercial Law. Companies also file with the FOPI financial reports on an individual basis. Companies must provide the FOPI with a reconciliation of the accounts if there are material differences between reports to shareholders or the public and reports filed with the FOPI. The FOPI collects a special report that gives details on any off-balance sheet obligations of insurance companies. According to the Commercial Law, each corporation, including an insurance company, must appoint an external auditor. Auditors must be independent. For larger companies, the provisions require that the auditor have certain credentials as well as experience in the field. The legislation provides the parameters for identifying the companies to which this rule applies. The FOPI does not approve the appointment of the auditor although it can object to the appointment of an auditor who it feels would not be sufficiently independent or competent to serve, and has done so in the past. Financial reports prescribed by the FOPI are not prepared on a consolidated basis, even though several of the licensed companies have many subsidiaries, some of which are not financial

	institutions.
Assessment	Observed.
Comments	The FOPI's internal analysis system enables the staff to compute approximately 50 early warning ratios on the supervised companies.
Principle 13.	**On-Site Inspection** The insurance supervisor should be able to: – carry out on-site inspections to review the business and affairs of the company, including the inspection of books, records, accounts, and other documents. This may be limited to the operation of the company in the jurisdiction or, subject to the agreement of the respective supervisors, include other jurisdictions in which the company operates; and – request and receive any information from companies licensed in its jurisdiction, whether this information be specific to a company or be requested of all companies.
Description	On-site inspections are conducted, but infrequently. Recent experience has suggested that inspections occur once in five years. The supervisors are organized in teams, covering the major areas of supervision. Every supervisor is assigned one or more insurance companies, for which he is the supervisory coordinator. The team, however, is collectively responsible for the results of supervision. The responsibility for insurance groups are kept within the same team. Every team has a coordinator who is responsible for the overall coordination of the activities. There is also a matrix of resource persons skilled in certain areas of expertise. This facilitates specialization and consistence of practice. The FOPI has the authority to request any information for supervisory purposes. The FOPI has executed trilateral agreements with each company, involving the FOPI, the company, and its external auditor. The agreements specify the scope for the work. Initially, the focus is on the annual review of assets to support technical provisions. However the scope for a particular assignment can be expanded if that seems appropriate. Auditors prepare a report for the shareholders but also a report to the Board indicating trends the company and the industry are facing. The auditors provide the Board report to the supervisors and will also provide the usual "management letter" if requested. Each year, the FOPI develops a program for inspections to be carried out the following year. The program identifies the risk issues that will be the focus of the forthcoming inspections. The program document adopts a modular approach, and each "module" serves as a type of procedures manual to outline what steps the inspectors are to take in respect of each of the identified risk areas. The program also identifies the "problem" companies that must be the target for inspections. A number of "routine" inspections are also included in each annual cycle. The program includes criteria for the selection of companies in each category. Although actual inspections are less frequent than would be desired (as a result of resource constraints), FOPI's supervision of companies has to be considered as the sum of all these measures, i.e. reports of auditors, including special reports and the trilateral agreements; detailed documents filed by companies; computer analysis performed using the TEDAP system; and the regular contact that staff maintain with company officials through correspondence and otherwise.
Assessment	Broadly observed.
Comments	It would be desirable that the FOPI be given the resources to substantially increase the frequency of on-site inspections since it is important that on-site inspections are carried out on a regular basis, in order to verify reported prudential information and to make other relevant observations regarding the operations of insurance companies.

Principle 14.	**Sanctions** Insurance supervisors must have the power to take remedial action where problems involving licensed companies are identified. The insurance supervisor must have a range of actions available in order to apply appropriate sanctions to problems encountered. The legislation should set out the powers available to the insurance supervisor and may include: – the power to restrict the business activities of a company, for example, by withholding approval for new activities or acquisitions; – the power to direct a company to stop practices that are unsafe or unsound, or to take action to remedy an unsafe or unsound business practice; and – the option to invoke other sanctions on a company or its business operation in the jurisdiction, for example, by revoking the license of a company or imposing remedial measures where a company violates the insurance laws of the jurisdiction.
Description	The officials at the FOPI have indicated that the supervisor has a range of remedial measures at its disposal, including change of management, revoking of licenses, restricting use of assets, etc. This wide range of actions are not, however, specified in the insurance legislation. According to the current insurance legislation, an insurance company can be fined up to SwF 5000 if it operates in violation of laws, ordinances or decrees. In less serious cases, the FOPI may issue a warning. The FOPI can apply administrative penalties on its own authority and this can include such measures as fines and temporary or permanent suspension of the authority to issue policies. For more serious problems, the FOPI will apply to a court for the application of more severe sanctions, such as the application of larger fines or withdrawal of license. The FOPI can also issue directions (cease and desist orders) to a specific company or to all companies, on its own authority. Actions taken by the FOPI are subject to appeal to a court.
Assessment	Broadly observed.
Comments	The FOPI should consider including in the new legislation more specific references to its powers to issue sanctions. It would be useful to develop and publish a "ladder of compliance" which makes more transparent the response that might be applied in response to a particular supervisory problem.
Principle 15.	**Cross-Border Business Operations** Insurance companies are becoming increasingly international in scope, establishing branches and subsidiaries outside their home jurisdiction, and sometimes conducting cross-border business on a services basis only. The insurance supervisor should ensure that: – no foreign insurance establishment escapes supervision; – all insurance establishments of international insurance groups and international insurers are subject to effective supervision; – the creation of a cross-border insurance establishment is subject to consultation between host and home supervisors; and – foreign insurers providing insurance cover on a cross-border services basis are subject to effective supervision.
Description	Foreign insurance establishments in Switzerland are subject to licensing by the Ministry of Justice and Police and supervision by the FOPI. Swiss insurance establishments abroad are not supervised by the FOPI but would be subject to supervision by authorities in the host jurisdiction Special arrangements have been negotiated with Liechtenstein that follows the home-country/host country understandings that are part of the Third Insurance Directive of the European Union**.**

Assessment	Broadly observed.
Comments	Swiss insurance companies are heavily involved in insurance operations abroad, both by branches and subsidiaries. For the sake of supervisory overview, it is essential to be able to monitor insurance activities carried out in other jurisdictions.
Principle 16.	**Coordination and Cooperation** Increasingly, insurance supervisors liaise with each other to ensure that each is aware of the other's concerns with respect to an insurance company that operates in more than one jurisdiction, either directly or through a separate corporate entity. In order to share relevant information with other insurance supervisors, adequate and effective communication should be developed and maintained. In developing or implementing a regulatory framework, consideration should be given to whether the insurance supervisor: – is able to enter into an agreement or understanding with any other supervisor both in other jurisdictions and in other sectors of the industry (i.e., insurance, banking, or securities) to share information or otherwise work together; – is permitted to share information, or otherwise work together, with an insurance supervisor in another jurisdiction. This may be limited to insurance supervisors who have agreed, and are legally able, to treat the information as confidential; – should be informed of findings of investigations where power to investigate fraud, money laundering, and other such activities rests with a body other than the insurance supervisor; and – is permitted to set out the types of information and the basis on which information obtained by the insurance supervisor may be shared.
Description	Under present statutes, the FOPI is not permitted to share confidential information with other supervisors. MOUs established to date have dealt with the ready exchange of non-confidential information. The exceptions relate to a number of special decrees negotiated with certain Swiss conglomerates. Under those decrees, and with the consent of the conglomerate and the insurance companies concerned, all types of information are shared as required among supervisors of banking in Switzerland and insurance and banking supervisors in other countries.
Assessment	Partly observed.
Comments	In order to carry out effective supervision of conglomerates and insurance companies with operation abroad, it is essential to be able to share supervisory information with other domestic supervisors and supervisors in other jurisdictions.
Principle 17.	**Confidentiality** All insurance supervisors should be subject to professional secrecy constraints in respect of information obtained in the course of their activities, including during the conduct of on-site inspections. The insurance supervisor is required to hold confidential any information received from other insurance supervisors, except where constrained by law or in situations where the insurance supervisor who provided the information provides authorization for its release. Jurisdictions whose confidentiality requirements continue to constrain or prevent the sharing of information for supervisory purposes with insurance supervisors in other jurisdictions, and jurisdictions where information received from another insurance supervisor cannot be kept confidential, are urged to review their requirements.
Description	Information given to the FOPI is considered confidential. Under employment rules applicable to all public servants, any information obtained in the course of their work must be treated as

	confidential and may not be disclosed. In practice, the FOPI distributes a considerable amount of data regarding the business of insurance companies. However this information is not considered "public" until the publication appears and any other unpublished information in FOPIs hands is not to be released to anyone.
Assessment	Observed.
Comments	The FOPI will be obliged to review its policy as Switzerland moves to a "freedom of information" approach. At that time, it will be obliged to identify very carefully those pieces of information that it collects that must not be revealed.

Table 8. Summary Observance of IAIS Insurance Core Principles

Assessment Grade	Principles Grouped by Assessment Grade	
	Count	List
Observed	6	6, 7, 8, 9, 12, 17
Broadly observed	6	1, 2, 10, 13, 14, 15
Partly observed	4	4, 5, 11, 16
Non-observed	1	3
Not applicable		

Recommended action plan and authorities' response to the assessment

Recommended action plan

- The authorities should move as quickly as possible to complete the preparation of the new insurance legislation.
- The compensation system for the FOPI staff should be reviewed and, if possible, separated from the general public service scales. Additional staff should be hired to increase the frequency of on-site inspections and to expand off-site monitoring of developments in the industry.
- The FOPI should be provided with broader authority to exchange confidential information with other financial sector supervisors.

Table 9. Recommended Action Plan—IAIS Core Principles

Reference Principle	Recommended Action
Principle 1. Organization of an Insurance Supervisor	Of a total staff of 55, the professional members of the FOPI dedicated to supervision number 35. The FOPI is anxious to increase staff in order to augment its supervisory capacity. It would be preferable if the general program of compensation recognized the special competencies required by all FOPI professional staff. The existing legislation is not very specific regarding the powers of the supervisor. The proposed new legislation is expected to make these powers more specific.
Principles 2-3. Licensing and Changes in Control	Fit and proper assessments are essential for the licensing process. This procedure is not presently carried out in Switzerland (except for licensing of foreign insurance companies.). Fit and proper issues are covered in the Draft Bill that will be submitted to the Government. The present law does not contain specific provisions relating to the assessment of owners and managers. Changes in control do not need to be approved, and the FOPI does not conduct assessments of managers or owners. As a principle, changes in control should be subject to the same scrutiny as the issuance of a new license. The supervisor should be empowered to block the transfer.
Principles 4-5. Corporate Governance and Internal Controls	The insurance legislation does not give directions regarding corporate governance. Since the FOPI has not provided formal guidance, no standards have been set in this area (except from the general provisions in the corporate legislation). International best practices for insurance companies would suggest that there be special duties specified for Boards of Directors in areas such as setting investment policy, risk management policy and the establishment and monitoring of a system of internal controls. The issue of formal guidelines in this respect would be an appropriate step for the supervisory authorities.
Principles 6-10. Prudential Rules	Investment controls will be improved and greater risk management achieved once effective internal control procedures are in place. New draft legislation will go beyond what is required by EU legislation and require consolidated supervision of insurance groups.
Principle 11. Market Conduct	In relation to consumer protection, it is essential that all who are involved in selling insurance products comply with some kind of ethical code. The FOPI could issue guidelines regarding codes of conduct and also suggesting that companies establish claims resolution procedures.
Principles 12-14. Monitoring, Inspection, and Sanctions	It would be desirable that the FOPI be given the resources to increase the frequency of on-site inspections since it is important that on-site inspections are carried out on a regular basis, in order to verify reported prudential information and to make observations regarding the operations of insurance companies.
Principles 15-17. Cross-Border Operations, Supervisory Coordination and Cooperation, and Confidentiality	The FOPI should continue and expand its practice of entering into MoUs with insurance supervisors in other jurisdictions (such as the one already in place with Liechtenstein) and also with supervisors of other types of financial institutions.

Authorities' response

The FOPI broadly agreed with this assessment, which it considered to be comprehensive, balanced, and constructive. At the same time, it wished to emphasize that most of the recommendations contained therein are being addressed in the proposed new legislation on insurance supervision.

IV. CPSS CORE PRINCIPLES FOR SYSTEMICALLY IMPORTANT PAYMENT SYSTEMS

Information and methodology used for assessment

This assessment pertains specifically to the interbank payment mechanism known as the Swiss Interbank Clearing (SIC). This real-time, gross settlement (RTGS) system is by far the most important payment mechanism in the country, and is a significant element of the global network of payment arrangements. The SIC handles both large- and small-value transactions. Participation in the SIC is open to a wide range of domestic and foreign financial institutions and clearing mechanisms. It is systemically important, and thus the subject of assessment according to the CPSS Core Principles for such systems.

The assessment was conducted based on information provided by the SNB in the form of the answers to the IMF questionnaire with regard to payment and securities clearing and settlement infrastructure, relevant sections of the current Federal Law on the Swiss National Bank (the LNB), the 2001 "experts" draft of the LNB, the SIC Users Manual, the SIC Rules and Regulations, and the October 8, 2001 draft of the Self-Assessment of the Core Principles for Systemically Important Payment Systems prepared by the SNB.[7] These sources were supplemented by discussions held with officials of the SNB, the chief executive officer of Swiss Interbank Clearing AG which is the principal computer-service corporation operating the SIC on behalf of the central bank, a senior official of SIS SegaInterSettle AG (SIS), Switzerland's central securities depository and securities settlement system, as well as individuals regularly using SIC at the two largest banks. The individuals involved in these discussions were both knowledgeable and cooperative. A fuller assessment of the payment system broadly defined was limited by the fact that time did not permit an examination of many of the other relevant laws such as the Swiss Civil Code, the Code of Obligations, or the bankruptcy law.

Institutional and market structure—Overview

As in many other countries, there are close links in the Switzerland between the payments system, the securities markets, and the foreign exchange market. The Swiss central securities depository (SIS) and its securities settlement system known as SECOM have been linked in real time to the SIC since 1995 in order to transfer funds and securities on a delivery-versus-payment basis. Together, the SIC and SIS form the platform for the daily implementation of monetary policy. The derivatives exchange, called Eurex, also settles over the SIC. The Swiss franc leg of foreign exchange transactions typically involves large-value payments moving between pairs of banks, via the SIC, two business days after spot purchase and sale contracts are negotiated.

[7] The main author of this assessment is James Dingle (Bank of Canada). The assessment is based on information available during the FSAP mission in October 2001.

The SIC is used for the regular settlement procedures of all the retail payment mechanisms, whether they are related to electronic payments at the point of sale, to checks, to bulk transfers of periodic payments such as salaries, interest and dividends, and, e.g., to regular debits of mortgage interest. The value of all these retail payment components represents only about 1 percent of the typical value of the daily flow of payments in the SIC.

Payment systems infrastructure

The Swiss Interbank Clearing (SIC) is unquestionably a systemically important payment system—both for Switzerland and for the global financial system. On an average day, electronic funds transfers amounting to some SwF180 billion are processed on a real-time, gross-settlement basis. (The *annual* value of Swiss GDP is, in comparison, SwF 407 billion). Of this daily average value, over half involves either foreign exchange transactions being settled, or the correspondent banking flows which reflect cross-border commercial and financial business payments. Each SIC transfer that passes the risk-control test of adequate balances in the sending participant's (continually updated) settlement account is immediately final (daylight overdrafts are automatically and legally prohibited). The SIC not only effects interbank transfers of funds, many of which are initiated by the clients of participating institutions, but it is also used for the cash settlement procedures of the securities clearing mechanism (SIS), the derivatives exchange (Eurex), and the bulk settlement arrangements of the various services reflecting retail-level payments (the interbank data media exchange called DTA, for example).

The broad usage of the SIC is reflected in its list of participants. At the end of 2000, there were 302 participating members, of which 55 functioned on a remote basis, many of these in turn being banks in other countries. Any Swiss bank or broker/dealer with a license from the Federal Banking Commission can gain access—essentially upon request—to the Swiss National Bank (SNB). Domestic or foreign clearing institutions will usually gain access if their presence will reduce systemic risk or enhance the significance of the Swiss financial center in the global context. Correspondingly the foreign banks that are users of these clearing institutions typically become SIC participants.

Principle-by-principle assessment

The following assessment of the Swiss Interbank Clearing is based on the guidance provided in the BIS document of 2001 titled Core Principles for Systemically Important Payment Systems, as well as the Guidance Note and Templates provided to the assessors by the International Monetary Fund.

Table 10. Detailed Assessment of Observance of CPSS Core Principles

Principle 1. The system should have a well-founded legal basis under all relevant jurisdictions.	
Description	Article 2 of the Law on the National Bank (LNB) describes the principal task of the Swiss National Bank (SNB) in a broad manner, as follows: "to regulate the country's money circulation, to facilitate payment transactions and to pursue a credit and monetary policy serving the interests of the country as a whole." In the particular case of the Swiss Interbank Clearing (SIC), contracts were put in place in order to allow the SNB to establish the operational arrangements for this system. First, a contract between the SNB and the Swiss Interbank Clearing AG, assigns rights and responsibilities to both the central bank and the corporation operating the SIC. For example, all changes being made to the SIC User Manual must be approved by the SNB. Second, a contract between the SNB and each institution participating in the system deals with the operation of each participant's SIC settlement account at the central bank. Third, there is a contract between SIC and each participant that commits each institution to follow the provisions of the SIC user manual and technical guidelines. There is no specific legislation governing the pledging of collateral, however the creation and perfecting of security interests is governed by the Civil Code and/or the Code of Obligations, a legal structure that has proved to be both sufficient and flexible. Rights of set-off are fully respected under Swiss law. There is no zero-hour law, hence allowing for real-time finality of payment in the SIC system. It is also worth noting that a law passed in 1999 allows for accounting by electronic means, stating that such records shall have the same evidentiary value as books and documents in written form. In 2000, an ordinance was enacted on the recognition of certification services.
Assessment	Observed.
Comments	The LNB is currently under revision, and it is expected that the role of the SNB as overseer of systemically important payment systems will become more formally defined in the new law.
Principle 2. The system's rules and procedures should enable participants to have a clear understanding of the system's impact on each of the financial risks they incur through participation in it.	
Description	The SIC is a real-time gross settlement (RTGS) system in which participants' multilateral positions are constrained such that they can never involve daylight overdrafts. Each settled transfer is final (unless misdirected and treated in the manner described in the SIC Rules and Regulations as summarized below). Consequently it is not risky for a bank to experience a substantial bilateral gain vis-a-vis another bank—even if that institution is experiencing financial difficulty. Information regarding the amount and beneficiary of each transfer that is not yet settled, but temporarily held in the sending bank's queue (because of insufficient settlement balances), is automatically provided to the receiving bank, a situation that facilitates intra-day liquidity management. On the other hand this information flow potentially also produces a risk of overly prompt crediting of the accounts of beneficiaries. (A beneficiary might immediately spend the funds in a manner that involves a final SIC transfer away from its bank.) The SIC Users' Manual states in Section B1 that a transfer held in a queue may be removed from the queue by the sending bank without the concurrence of the receiving bank until 15:00 hours (or 3 p.m.); thereafter the receiving bank must agree to the removal. This provision balances the intra-day liquidity management needs of the two institutions, both of which may have been acting on the assumption that the transfer would shortly be settled and hence become final. The SIC Rules and Regulations state in Section 2.6 that a settled but erroneously directed

	transfer may, upon written request from the sending bank, be immediately returned by the receiving bank.
Assessment	Observed.
Comments	The current draft of the new Federal Law on the Swiss National Bank formalizes in Article 18 the SNB's operating arrangements for, and oversight of, the SIC. Moreover, the central bank would be able to demand that minimum requirements be fulfilled by any system from which risks for the stability of the financial system emanate. Requirements could involve the organizational basis, the business conditions, the payment medium used, the operational security, the criteria for access by participants, the implications of illiquidity on the part of a participant, and the reporting of statistics. The operators of the system would be obligated to provide the SNB, on request, with all necessary additional information.
Principle 3. - The system should have clearly defined procedures for the management of credit risks and liquidity risks, which specify the respective responsibilities of the system operator and the participants and which provide appropriate incentives to manage and contain those risks.	
Description	Because the SIC calculates each bank's position on a real-time, payment-by-payment basis, it automatically prevents daylight overdrafts, and uses accounts at the central bank as the settlement asset, no credit risk arises in the system for the private participants. Three tools are available to support the management of liquidity risk by the banks: queuing; an intra-day credit facility; and the overnight Lombard credit facility. The details follow. (i) Any attempted payment that exceeds the value of the current position of the bank in question will be placed in the out-going queue of that institution. As soon as the bank's position is increased sufficiently, the queued payment will—if it is at the head of the queue—be settled and released into the position of the receiving bank. Both outgoing and incoming queues are visible to the banks in question, including the identity of the beneficiary. (This latter aspect helps the receiving bank forecast whether the funds will rest on deposit, or be disbursed to another institution later in the same day.) (ii) Banks can obtain intra-day credit from the beginning of the daily cycle until 14:45 hours (or 2:45 p.m.). Once collateral is pledged to the SNB, the funds are provided immediately. Repayment may be initiated beginning at 15:00 hours (3 p.m.). If repayment has not occurred by 16:15 (2:15 p.m.), an interest charge that exceeds the overnight rate by twice the Lombard surcharge (i.e., by 400 basis points) applies. (iii) If faced with a persistent liquidity shortage as the day comes to a close, domestic participants in the SIC may draw on the Lombard facility of the SNB. The amount that may be so borrowed is limited only by the amount of eligible securities that may be pledged by the bank in question. The rate on Lombard loans is 200 basis points over the overnight rate.
Assessment	Observed.
Comments	
Principle 4. The system should provide prompt final settlement on the day of value, preferably during the day and at a minimum at the end of the day.	
Description	The SIC is a real-time gross settlement (RTGS) system. Any SIC transfer that is not held in a queue is immediately and finally settled. (Please note the treatment of misdirected transfers described under Core Principle 2, above.) The receiving bank can then make a corresponding credit to the beneficiary's account without exposing itself to any risk associated with the beneficiary's subsequent disbursal of the funds.
Assessment	Observed.
Comments	

CP V - A system in which multilateral netting takes place should, at a minimum, be capable of ensuring the timely completion of daily settlements in the event of an inability to settle by the participant with the largest single settlement obligation.	
Description	The SIC is described as a real-time gross settlement system.
Assessment	Not applicable.
Comments	
Principle 6. Assets used for settlement should preferably be a claim on the central bank; where other assets are used, they should carry little or no credit risk and little or no liquidity risk.	
Description	The assets used for settlement purposes in the SIC are effectively claims on the Swiss central bank. During the daily operations of the SIC, the evolving positions of each bank are calculated and maintained within the computer systems of SIC AG, a private corporation which is acting as agent for the SNB pursuant to the contracts described below under Principle 10. The central bank has full information about the flows of settled payments, exactly as it would if it were its own computer systems performing the real-time calculations.
Assessment	Observed.
Comments	
Principle 8. The system should ensure a high degree of security and operational reliability and should have contingency arrangements for timely completion of daily processing.	
Description	Continuous efforts have been made to further strengthen the security package of the SIC, despite the fact that operations have not been hampered by fraud or attack in over 15 years. IBASEC (INterBAnk SECurity System), a security package with state-of -the-art authentication and encryption devices, was implemented in 1999. The SIC is highly reliable. Once a year the audit section of Telekurs Holding AG (the parent company of SIC AG) arranges for an accounting firm to conduct an operations and security audit of the system. To date these investigations have not identified any major shortcomings, although gaps in the key management procedures were pointed out. Contingency arrangements, including internal and external emergency committees, exist and are tested regularly. These cover three types of situations: (i) a breakdown of a participant; (ii) a breakdown of the host system at SIC AG; and (iii) a complete system failure such as an unrecoverable software error. The details in each case form sections of the SIC User Manual. There is an offline, gross settlement, batch processing system for back-up purposes should the SIC prove unavailable for a significant interval. It is called MINI SIC, and it is tested each year with compulsory involvement in the part of all domestic participants.
Assessment	Observed.
Comments	
Principle 8. The system should provide a means of making payments which is practical for its users and efficient for the economy.	
Description	The users of the SIC are the central bank, all banks operating in Switzerland whether domestic or foreign, many broker/dealers, and a number of clearing and settlement mechanisms processing transactions in a variety of financial products. In 2000, the financial arm of the Swiss post office, itself a major supplier of retail-level payment services, became a participant in the SIC. All these constituencies benefit from the immediate finality of SIC transfers in terms of minimizing payment-related risks in their particular contexts. The efficiency with which the SIC provides services to its users is partially a result of the fact that, before major development projects are undertaken, a business case is investigated. Over

	time, the supporting private corporation has been profitable (within the contractual constraint that revenues should not continually or substantially exceed costs). The participants' fees for payment transfers are comparable to those observed in other national RTGS systems.
Assessment	Observed.
Comments	
Principle 9. The system should have objective and publicly disclosed criteria for participation, which permit fair and open access.	
Description	Access to the SIC depends primarily on the granting of a settlement account at the SNB. Since the central bank is obligated to open such an account for any Swiss bank or broker/dealer that requests access, any institution in these two categories will gain access after the related communications have occurred. In the cases of other Swiss financial institutions (including Postfinance, an arm of the federal post office), and both Swiss and foreign clearing and settlement organizations, the SNB will open the necessary settlement account if it judges that such a development would either reduce systemic risk, or be of positive significance for Switzerland as a financial center. Participants of the SIC wishing to operate on a remote access basis, that is, by means of computer/communications linkage from outside the country, must meet additional requirements relating to adequate supervision (in the case of banks and broker/dealers), and the "reachability" of personnel capable of expressing themselves clearly in English, French, or German and accessible during normal business hours in Central European Time. All remote applicants have to prove their technical capability prior to joining the live SIC, provide information demonstrating the nature of their countries' telecommunications infrastructures' support for messages to and from Switzerland, and show they participate in the anti-money-laundering initiatives required by their own supervisory authorities. In summary, these access criteria, which are published in descriptive articles on the central bank's website, imply that the SIC is among the most open large-value funds transfer systems of the world.
Assessment	Observed.
Comments	
Principle 10. The system's governance arrangements should be effective, accountable and transparent.	
Description	The governance structure of the SIC involves two major components: the SNB which concentrates on the broad policy questions of payment system design; and the Swiss Interbank Clearing AG, which is a technical services corporation handling the operational structure under a contract with the SNB. (This contract resembles an outsourcing contract.) The central bank is represented on the Board of SIC AG by the Director of the Informatics and General Processing Division of Department III. The contractual agreement between the SNB and SIC AG covers the following topics: the cost recovery objective; the structure of fees paid by participating institutions; the allocation of liability including sanctions; and the monthly reporting responsibility of the service provider. In addition the SNB has access to all internal and external audits conducted at SIC AG, it can carry out on-site inspections, and it can require the replacement of incompetent staff. Two sections of the SNB (each staffed by five persons) are directly involved with the operations and evolution of the SIC. The first section manages the daily cycle of SIC operations, determining any changes to the usual start and stop sequences, manages the settlement accounts of the participants, and is in a position to effect payments for an institution that is unable to do so itself for technical reasons. The second section deals with

	policy and oversight issues, bearing in mind both systemic risk and the daily implementation of monetary policy. The governance arrangements of the SIC continue to function well. The system is sophisticated, it has been reliable, and the service corporation SIC AG has been profitable.
Assessment	Observed.
Comments	
Central Bank Responsibilities in applying the CPSIPS	
Responsibility A. The central bank should define clearly its payment system objectives and should disclose publicly its role and major policies with respect to systemically important payment systems.	
Description	The SNB's involvement in the payment system is based on the Law on the National Bank which specifies the "facilitation" of payment transactions as one of its three major responsibilities. In this context its primary objectives are "efficiency" and "safety." The SNB uses a market-based approach in pursuing the first objective, encouraging market forces to play their role in developing, operating and enhancing payment-system infrastructure. The SNB focuses on the one systemically important system in its pursuit of the second objective. It is proactive in its oversight of the SIC, maintaining an ongoing professional and contractually governed relationship with SIC AG, the computer-service provider for the system. The objectives of the SNB are publicly disclosed in a variety of ways, the text displayed on the inside front cover of the 2000 Annual Report a good example.
Assessment	Observed.
Comments	The SNB is currently drafting a payment system policy paper that will describe the central bank's objectives, roles and major policies. It will be published on the Bank's website (http://www.snb.ch) after endorsement by the Governing Board.
Responsibility B. The central bank should ensure that the systems it operates comply with the core principles.	
Description	The contractual documents governing the relationship between the SNB and SIS AG state that the latter operates the system "on behalf of the central bank." (The SNB is the overseer, and it has one seat on the Board of the service corporation.) Thus it is appropriate to view the SIC as a system that is not operated by the central bank.
Assessment	Not applicable.
Comments	
Responsibility C. The central bank should oversee observance with the core principles by systems it does not operate and it should have the ability to carry out this oversight**.**	
Description	The SNB oversees the SIC in a variety of ways. The contracts between the central bank and the service-providing corporation clearly delineate the rights and responsibilities of each party. The SNB has one seat on the Board. The SNB can grant particular institutions access to the system. All changes to the SIC operating rules and procedures are approved by the SNB. All design changes are similarly approved. The central bank approves the level of transactions fees, reviews the internal governance structures, receives all internal audit reports and can request external audits. It can inspect the safety of the operational facilities, and can have incompetent personnel removed.
Assessment	Observed.
Comments	The forthcoming Law on the Swiss National Bank is expected to formalize the oversight of any electronic payment system. This power would extend to any company incorporated in a foreign country and operating such a system in Switzerland. It is thus likely that the SNB will

	shortly have to increase (by one intensity level) its monitoring of the euroSIC, a "quasi-system" which is operated by the Swiss Euro Clearing Bank, a recently established bank in Frankfurt that facilitates euro payments within Switzerland and in Europe generally. (The higher level of monitoring would not be the formal oversight of a systemically important payment system.)
Responsibility D. The central bank, in promoting payment system safety and efficiency through the core principles, should cooperate with other central banks and with any other relevant domestic or foreign authorities.	
Description	The SNB meets regularly with the Federal Banking Commission to ensure an adequate exchange of information on the development and operation of the various payment mechanisms in Switzerland. Internationally, the SNB participates actively in the BIS Committee on Payment and Settlement Systems. The SNB maintains bilateral relationships with numerous central banks and other authorities or organizations with interest in payment system matters.
Assessment	Observed.
Comments	

Table 11. Summary Observance of CPSS Core Principles

Assessment grade	Principles grouped by assessment grade	
	Count	List
Observed	9 3	CP I, II, III, IV, VI, VII, VIII, IX, and X; Responsibilities A, C, and D.
Broadly observed		
Partly observed		
Non-observed		
Not applicable	1 1	CP V Responsibility B

Recommended action plan and authorities' response to the assessment

Table 12. Recommended Action Plan—CPSS Core Principles

Reference principle	Recommended action
Security and operational reliability, and contingency arrangements	
Principle 7	The SNB should analyze developments that are either planned or anticipated to occur during 2002, examining the contingency procedures of the SIC and the extraordinary liquidity sources of relevant currencies in plausible situations involving interruptions of operations in both the traditional and in the new (continuous linked) arrangements for foreign exchange settlements. The SNB should continue to prepare for operational problems related to violent acts. The SNB should consider hiring an accounting firm of its own choice to conduct occasional operations and security audits of the SIC.
Central Bank responsibilities in applying the Core Principles	
Responsibilities A-D	The SIC should continue its interaction with the Deutsche Bundesbank with respect to the evolution of the euroSIC, in a manner consistent with the Lamfalussy Principles of Cooperative Central Bank Oversight of Cross-Border Netting and Settlement Systems.

Authorities' response

The staff of the SNB has begun the recommended examination of the structural developments anticipated in 2002, and has investigated the steps necessary to establish an inter-central bank swap arrangement that could provide U.S. dollar liquidity if needed. The suggestions made with respect to operational reliability and additional security audits have been viewed positively.

V. IMF CODE OF GOOD PRACTICES ON TRANSPARENCY IN MONETARY AND FINANCIAL POLICIES

This assessment was prepared as part of the Financial Sector Assessment Program (FSAP) of Switzerland. Its purpose was to assess observance of the IMF developed Code of Good Practices on Transparency in Monetary and Financial Policies ("Code"). For purposes of the code, transparency refers to an environment in which policy objectives, their legal, institutional and policy framework, monetary and financial policy decisions and their rationale, data and information related to these policies, and the terms of central bank accountability are provided to the public in a comprehensible, accessible and timely manner.

The assessment of observance of each practice is made on a qualitative basis using a five-part assessment system: **observed, broadly observed, partly observed, non-observed** and **not applicable**. A practice is considered **observed** whenever all essential criteria are met without significant deficiencies—though there may be instances where a country can demonstrate a practice is observed through different means. A practice is considered **broadly observed** whenever only minor shortcomings are observed, which do not raise any concerns about the ability to achieve full observance with the principle within a prescribed period of time. A practice is considered **partly observed** whenever, despite progress, the shortcomings remain substantial. A practice is considered **non-observed** whenever no substantive progress toward observance has been achieved. A practice is considered **not applicable** whenever, in the view of the assessor, the practice does not apply given the structural, legal and institutional features of a jurisdiction.

A. Transparency of Monetary Policy

Information and methodology used for assessment

The assessment contained in this chapter is based on discussions with the staff of the SNB, responses to questionnaires sent to the authorities, and an analysis of the National Bank Law (NBL), other relevant laws, regulations, administrative policies, and information provided during these meetings. This assessment was prepared by Anastassios Gagales and Maike Luedersen (both IMF). It is based on information available during the FSAP mission in October 2001.

The mission also discussed the proposed revisions to the National Bank Law (revNBL), which is currently in the consultation process. A draft bill, incorporating comments made in the consultation process, is expected to be submitted to Parliament in mid-2002. The revisions are anticipated to take effect in 2004 at the earliest.

Institutional and market structure-overview

In Switzerland, the responsibility for monetary policy is vested with the SNB. In 2000, after a quarter century of monetary targeting, the SNB made several changes, among them: (i) it switched to a new framework in which monetary policy is set on the basis of the inflation forecast over a three-year horizon with an explicit objective of keeping medium-term inflation below 2 percent; (ii) it also introduced as an operational target a publicly announced range for the three-month Swiss franc rate; and (iii) adopted repos as the main instrument of controlling liquidity.

Practice-by-practice assessment

Table 13. Detailed Assessment of Observance of Transparency Code—Monetary Policy

I. Clarity of Roles, Responsibilities and Objectives of Central Banks for Monetary Policy	
1.1	**The ultimate objective(s) and institutional framework of monetary policy should be clearly defined in relevant legislation or regulation, including, where appropriate, a central bank law.**
Description	The ultimate objective and institutional framework of monetary policy are defined in the Federal Constitution (Constitution) and the National Bank Law (NBL). The Swiss National Bank (SNB), as an independent central bank, is in charge of monetary policy and shall pursue a monetary policy serving the interests of the country as a whole (art. 99 Constitution and art. 5 NBL). However, neither the Constitution nor the NBL explicitly address maintaining price stability as ultimate objective. The SNB, however, regards maintaining price stability as the ultimate objective of Swiss monetary policy and this interpretation has not been challenged. The NBL specifies (i) the SNB's corporate structure (arts. 1-13, 25-27 NBL); (ii) the monetary and foreign exchange policy, the SNB's scope of business, the central bank instruments and the note-issuing privilege (arts. 1, 14-16k, 66-68); (iii) its organization and the cooperation with the federal administration (arts. 28-63); and (iv) procedural provisions and criminal sanctions (arts. 65a-65d, 68a, 69). The responsibility for determining and implementing Switzerland's monetary policy is vested

	in the SNB's Governing Board (Governing Board). The Governing Board is the supreme managing and executive body of the SNB and represents the SNB vis-à-vis the public. The Governing Board is in particular responsible for the conceptional and operational monetary policy decisions, determining the level of monetary reserves, the investment of assets, and the exercise of competencies relating to monetary and foreign exchange policy (art. 16j NBL).
Assessment	Observed.
Comments	The proposed revised NBL will more precisely establish maintaining price stability as the ultimate objective in the law and will establish that the SNB shall pursue a monetary policy serving the overall interests of the country. It shall ensure price stability. In doing so, it shall duly take into account the development of the business cycle (art. 5 revNBL). The proposed provision should not, however, be interpreted that the SNB guarantees price stability.
1.1.1	The ultimate objective(s) of monetary policy should be specified in legislation and publicly disclosed and explained.
Description	As noted above, the objective of monetary policy is specified in the Constitution and the NBL. Both documents are publicly disclosed and easily available, including on the websites maintained by the SNB and Swiss federal authorities, respectively (http://www.snb.ch). The SNB regards maintaining price stability as the ultimate objective of Swiss monetary policy and consistently disseminates this interpretation in official bulletins, reviews, speeches, and annual reports.
Assessment	Observed.
Comments	
1.1.2	The responsibilities of the central bank should be specified in legislation.
Description	The responsibilities of the SNB are specified in the NBL. The SNB conducts the country's monetary policy (art. 2, para. 1 NBL), facilitates the interbank payment system and ensures its safety (art. 2, para. 1 NBL), ensures money supply (art. 2, para. 1 NBL), invests monetary reserves (art. 14 NBL), advises the federal authorities on issues of economic policy (art. 2, para. 1 NBL), acts as banker to the government (art. 15 NBL), promotes stability in the financial system (arts. 98, 99 Constitution, art. 2 NBL), and compiles statistics (arts. 7, 9 Banking Law). The SNB may act as a lender of last resort in case of liquidity crisis, but there is no specific provision on emergency lending in the NBL.
Assessment	Observed.
Comments	The proposed revised NBL will establish the following tasks for the SNB: to supply the Swiss franc money market with liquidity, ensure the provision and distribution of cash money, facilitate and secure the operation of cashless payment systems, and manage the monetary reserves (art. 5, para. 2 revNBL). Furthermore the SNB will participate in international monetary cooperation and act as banker to the Confederation (art. 5, para. 3,4 revNBL). The proposed revised NBL will also provide a clear basis for the collection of statistical data from banks, exchanges, securities dealers and fund managers of Swiss investment funds and representatives of foreign investment funds (possibly extended to other entities such as insurance companies, pension funds, investment funds and holding companies, operators of payments systems and the postal service (arts. 14, 15 revNBL)). Although not expressly stated, the lender-of-last-resort function is understood to be captured in article 5, para. 2(a) revNBL.
1.1.3	The legislation establishing the central bank should specify that the central bank has the authority to utilize monetary policy instruments to attain the policy objective(s).
Description	The NBL sets out in detail the instruments to implement monetary policy (arts. 14-16k NBL). The description of the SNB's scope of business is quite detailed in the law and includes the discounting of bills, cheques and treasury bills issued by the Confederation, cantons or municipalities; buying and selling of, as well as dealing under a repurchase agreement in,

	treasury bills and debt certificates of the Confederation; issuing and repurchasing of, including dealing under a repurchase agreement in, its own interest-bearing debt certificates with a period to maturity not exceeding two years, in so far as this is necessary for the purposes of an open-market policy; buying and selling (cash or forward) of, as well as dealing under a repurchase agreement in, bills and cheques drawn on payees abroad, debt certificates of foreign states, international organizations and foreign banks, derivatives (options, futures, forward rate agreements), in so far as these are designed to regulate market risks on debt certificates and balances in foreign countries; granting interest-bearing current-account advances at up to ten days' notice against security in the form of Swiss debt certificates, federal debt register claims, discountable bills and gold (advances against collateral). Shares and participations in cooperatives are not eligible as security for such advances; entering into time-limited discount and Lombard commitments for claims and securities that are eligible for discount or as collateral; accepting deposits on non-interest-bearing accounts; carrying out giro, clearing and collection transactions; opening correspondent accounts with domestic and foreign banks; selling Swiss and foreign cheques; buying and selling of, as well as dealing under a repurchase agreement in, gold for its own account or for the account of third parties; issuing gold certificates; accepting in custody and managing securities and valuables, buying, selling and subscribing securities for the account of third parties; acting as a subscription agent for bond issues of the Confederation, the cantons, enterprises guaranteed by a canton and the central mortgage institutions, but excluding participation in the firm underwriting of bonds; and buying and selling international payment instruments.
Assessment	Observed.
Comments	The proposed revised NBL will describe the instruments in a more general and comprehensive way, thereby enhancing flexibility. The NBL may open interest bearing and non-interest bearing accounts for banks and other financial market participants, and take into custody assets; open accounts with banks and other financial market participants; become active in financial markets by buying and selling Swiss franc or foreign currency denominated receivables and securities as well as precious metals and claims on precious metals (spot or forward) or by entering into lending operations therewith; issue and repurchase own interest bearing bonds (spot and forward) as well as create derivatives on receivables, securities and precious metals; enter into credit transactions with banks and other financial market participants, on condition that sufficient collateral is provided for the loans; hold and manage assets; and enter into relations with foreign central banks and international organizations and effect with them all kinds of banking transactions, including raising and granting credits in Swiss francs, foreign currencies and international payment instruments (arts. 9, 10 revNBL).
1.1.4	Institutional responsibility for foreign exchange policy should be publicly disclosed.
Description	Under the current system of flexible exchange rates the responsibility for the external value of the Swiss franc is attributed to the SNB. The SNB is independent in conducting monetary policy (art. 99, para. 2 Constitution; art. 2, para. 1 NBL), and the exchange rate reflects independent monetary policy decisions. The German version of the NBL is explicit in this sense, as it refers to "*Kredit- und Währungspolitik.*" In the French version of the NBL, it is understood that monetary policy necessarily includes foreign exchange policy. The institutional responsibility for changing the exchange rate regime cannot, however, be found in one single legal provision. Institutional responsibility is explicitly explained in the explanatory notes accompanying bills of the Federal Council (*Botschaften*), for example, in the bill regarding the Federal Law on Currency and Legal Tender (admin.ch/ch/d/ff/1999/7258.pdf, Chapter 211, para. 2). Two separate cases are to be distinguished: -- A decision to permanently peg the Swiss franc under international law would require action by the Parliament (art. 166, para. 2 Constitution). The Federal Council is in charge of negotiation and ratification of treaties and submits them to the Parliament for approval (art. 184 Constitution). -- A decision to unilaterally peg the Swiss franc to another currency or basket of currencies

	would be a monetary policy decision of major importance and, therefore, would require consultations between the SNB and the Federal Council (art. 2, para. 2 NBL).
Assessment	Observed.
Comments	It is desirable to specify in law the allocation of institutional responsibility for determining the exchange rate regime.
1.1.5	The broad modalities of accountability for the conduct of monetary policy and for any other responsibilities assigned to the central bank should be specified in legislation.
Description	The SNB is accountable to the Federal Council, and the Federal Council must approve the annual report and annual accounts (art. 63, para. 2(i) NBL). The law requires that an annual report be prepared, approved by the shareholders' meeting (art. 37, para. 1 NBL) and published (art. 25, para. 3 NBL).
Assessment	Observed.
Comments	The proposed revised NBL will set out the SNB's accountability in a much more detailed manner and will distinguish between accountability, which is limited to the relationship with the Federal Council, and sharing information with the competent parliamentary committee and the public at large (art. 7 revNBL). The SNB will explain to Parliament the economic situation as well as its monetary policy and provide information to the public at least once a year. The SNB will produce and publish quarterly reports on economic and monetary developments and publish weekly data of importance to monetary policy. Although covered by stock exchange regulations, which require that all listed firms publish annual reports, it is recommended that the proposed revised NBL should contain a provision explicitly requiring the publication of the annual report.
1.1.6	If, in exceptional circumstances, the government has the authority to override central bank policy decisions, the conditions under which this authority may be invoked and the manner in which it is publicly disclosed should be specified in legislation.
Description	The government has no authority to override SNB's policy decisions. It is clearly set out in the Constitution that the SNB is independent (art. 99 Constitution).
Assessment	Not applicable.
Comments	The proposed revised NBL will mirror the provision of the Constitution and explicitly state the independence of the SNB (art. 6 revNBL).
1.1.7	The procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing body of the central bank should be specified in legislation.
Description	The three members of the SNB's top managing and executive body, the Governing Board, are elected by the Federal Council on the recommendation of the Bank Council for a period of six years (art. 53 NBL). A reelection is possible. The members of the Governing Board (as well as the members of other SNB organs and SNB staff) must be Swiss citizens (art. 55 NBL). They may not be members of the federal parliament, a cantonal government or the Bank Council at the same time (art. 56 NBL). The federal government has the power to dismiss members of the Governing Board. The NBL does not identify specific grounds for removal, but requires that the reasons be explained (art. 60 NBL).
Assessment	Partly observed.
Comments	The proposed revised NBL requires that members of the Governing Board must have knowledge in banking and financial issues. It does not, however, require that members be "fit and proper" individuals (for example, a comparable requirement exists in article 3, para. 2(c) Banking Law). The proposed revised NBL will specify in legislation the grounds for removal of members of the Governing Board in that a member of the Governing Board or deputy may be removed

	during their tenure by the Federal Council on the request of the Bank Council if the person no longer fulfills the conditions for exercising its position or committed a grave offense (art. 42, para. 1 revNBL). In this context, it would be advisable to be more specific regarding the criteria to be applied to determine that a person no longer fulfills the conditions for exercising its position. In particular, by referring to "preconditions," such criteria appear limited to the requirements set out in article 41 revNBL. However, these factors may not be the most relevant for a removal from office.
1.2	**The institutional relationship between monetary and fiscal operations should be clearly defined.**
Description	There is no institutional relationship specifically defined for the conduct of monetary and fiscal operations since the SNB is independent. The institutional relations in general between the federal government and the SNB are defined as follows: (i) the SNB is administered with the participation and under the supervision of the Confederation (art. 1, para. 2 NBL); (ii) before important decisions regarding the business cycle and monetary policies are taken, the Federal Council and the SNB inform each other of their intentions and exchange views (art. 2, para. 2 NBL); (iii) the federal authorities exercise oversight mostly through the exercise of specific competencies granted to the Federal Council (art. 63 NBL).
Assessment	Observed.
Comments	
1.2.1	If credits, advances, or overdrafts to the government by the central bank are permitted, the conditions when they are permitted, and any limits thereof, should be publicly disclosed.
Description	The NBL does not explicitly prohibit credit to the government. However, the NBL limits any overdrafts to the amounts kept by the government in accounts with the SNB (art. 15, para. 1 NBL).
Assessment	Observed.
Comments	The proposed revised NBL will explicitly state that the SNB may not extend any credit to the government (other than intraday overdrafts against sufficient collateral) and prohibit the acquisition of new issues of government securities in the primary market (art. 11, para. 2 revNBL). The proposed revised NBL does not set an upper limit for such intraday overdrafts.
1.2.2	The amounts and terms of credits, advances, or overdrafts to the government by the central bank and those of deposits of the government with the central bank should be publicly disclosed.
Description	This information is provided only in the "notes to the accounts" section of the SNB's annual report. SNB's periodic statements (every 10 days) provide information only on deposit liabilities to, but not on claims (credits, securities) on the Confederation.
Assessment	Observed.
Comments	The SNB does not grant credit to the Confederation. In the event of liquidity bottlenecks, the SNB assists the Confederation to borrow from banks or debits the time deposits that the Confederation holds with the SNB. It is desirable to disclose in the 10-day statements any credits to the general government (see 3.2.1 below).
1.2.3	The procedures for direct central bank participation in the primary markets for government securities, where permitted, and in the secondary markets, should be publicly disclosed.
Description	The NBL does not explicitly prohibit credit to the government, but the SNB does not participate in the primary markets other than as agent in issuing government securities. The SNB may purchase government securities on the secondary market. There is no provision in the law limiting such purchases. The Annual Report explains the guidelines for participation in the secondary market. Currently, the SNB pursues a passive investment strategy, the objective being to reproduce an index for Swiss franc bonds that is representative of the market. Internal

	operational procedures are not disclosed to the public.
Assessment	Observed.
Comments	The proposed revised NBL will explicitly prohibit the acquisition of new issues of government securities in the primary market (art. 11, para. 2 revNBL). It will explicitly provide for the buying and selling of securities in the secondary market (art. 9, para. 1(c) revNBL). It is desirable to disclose in the 10-day statements the holdings of general government securities (see 3.2.1 below).
1.2.4	Central bank involvement in the rest of the economy (e.g., through equity ownership, membership on governing boards, procurement, or provision of services for a fee) should be conducted in an open and public manner on the basis of clear practices and procedures.
Description	The scope of activities of the SNB are exhaustively listed in article 14 NBL. These activities do not include the purchase of securities (other than government securities). The SNB is not actively involved in the rest of the Swiss economy other than for activities related to its primary task. The SNB holds shares in the BIS, is a shareholder in a company engaged in the printing of banknotes, and is involved in a center for economic and monetary research at Gerzensee. The SNB is also represented on the management board of Swiss Interbank Clearing, a payments system provider.
Assessment	Observed.
Comments	In the late 1970s, the SNB ceased providing preferential financing to the private sector and private banking facilities (other than for employees).
1.2.5	The manner in which central bank profits are allocated and how capital is maintained should be publicly disclosed.
Description	The rules governing the distribution of profits are based on art. 99 Constitution and art. 27 NBL. Out of the net profit as shown in the income statement, an amount which may not exceed 2 percent of the share capital is appropriated to a reserve fund and a dividend not exceeding 6 percent of the paid-up capital is then paid to the shareholders. Thereafter, the cantons receive an amount of 80 centimes per capita. Of the remainder, two-thirds and one-third, respectively, are allotted to the cantons and the Confederation. While profit distribution is laid down in detail in the law (art. 27 NBL), no regulations exist for calculation of the net profit and the level of reserves required from an operational and economic point of view. For several decades, earnings were mostly used for accumulating reserves, and no excess was available to be distributed to the cantons and Confederation. At the beginning of 1992, the federal government and the SNB addressed this issue of growing foreign exchange reserves by linking the increase in future unsecured currency reserves to the growth in nominal gross national product. Although the earnings situation of the SNB varies considerably, annual payments were limited to a maximum of SwF 600 million and higher earnings would lead to higher growth in reserves. In April 1998, a new agreement between the Federal Department of Finance and the SNB on the distribution of profits was entered into. It provides for a constant annual distribution of SwF 1,500 million to the cantons and the Confederation over the next five business years (1998-2002). If the reserves fall below a level of 60 percent of the targeted reserves, the distributions must be reduced or eliminated altogether. The agreement is not publicly disclosed, but the procedure is described in annual reports (1991, p. 65; 1992, p. 66-67; 1993, p. 69) and in the quarterly bulletin 1998, p. 59. In March 2002, a new agreement for the distribution of profits was concluded for 2003-12 that also amended the 1998 agreement. The new terms stipulate an extraordinary transfer of SwF 1 billion in business year 2002 and a constant annual distribution of SwF 2.5 billion to the cantons and the Confederation over the next 10 business years. The increase in distributed profits is linked to the gradual reduction of excess provisions at the SNB (the SNB has made

	the determination that its provisions at end-2001 exceeded the optimal level by SwF 11 billion). The new agreement provides that the SNB will expand its reserves at the same pace as nominal GDP over the past five years. If the targeted level of reserves is missed by SwF 10 billion or more the distribution of profits would be reduced accordingly or eliminated; likewise, if the reserves exceed their targeted level by SwF 10 billion or more, the distribution of profits could be raised. The amount for distribution in the period 2007-12 will be reviewed in 2007. The agreement is not publicly disclosed, but is described in a joint press communiqué of the SNB and the Federal Department of Finance and in SNB's Annual Report.
Assessment	Observed.
Comments	The proposed revised NBL will simplify the procedure for distribution of profits. The SNB shall determine the amount of currency reserves necessary for conducting monetary policy taking into account the development of the Swiss economy (art. 27 revNBL). A dividend not exceeding 6 percent of the paid-up capital is then paid to the shareholders and, thereafter, two-thirds and one-third, respectively, of any remaining net profits are allotted to the cantons and the Confederation (art. 28 revNBL).
1.3	**Agency roles performed by the central bank on behalf of the government should be clearly defined.**
Description	The responsibilities of the SNB as a government agent are defined in the NBL and described below under 1.3.1.
Assessment	Observed.
Comments	
1.3.1	Responsibilities, if any, of the central bank in (i) the management of domestic and external public debt and foreign exchange reserves, (ii) as banker to the government, (iii) as fiscal agent of the government, and (iv) as advisor on economic and financial policies and in the field of international cooperation, should be publicly disclosed.
Description	The responsibilities of the SNB as a government agent are set out in the NBL (art. 2, para. 3 NBL). The SNB is not involved in the management of the domestic or external public debt other than maintaining the federal register (art. 15, para. 1 NBL). Switzerland's foreign exchange reserves under the relevant laws are part of SNB's balance sheets and it is understood that they be managed by the SNB itself. The SNB acts as banker to the government, in particular keeps its accounts and executes payments (art. 15 NBL). However, there is no obligation for the government to maintain all accounts with the SNB. The SNB places short term money of the government in the market and advises the federal government in banking activities. The SNB also acts as an agent in the issuance of government bills and bonds (art. 14, para. 13 NBL). The SNB also advises the federal authorities in monetary matters (art. 2, para. 1 NBL). This mandate is understood in a comprehensive manner and includes various aspects of economic policy and financial regulation. SNB also cooperates with the Federal Council in international monetary cooperation, such as representation at the International Monetary Fund, and serves as advisor in this regard.
Assessment	Observed.
Comments	The proposed revised NBL will explicitly provide for the management of the foreign exchange reserves (art. 5, para. 2(d) revNBL) and the cooperation of the SNB with the Federal Council in international monetary cooperation (art. 5, para. 3 revNBL). It will also allow for reasonable remuneration for services performed by the SNB as banker to the government (art. 11, par. 1 revNBL).

1.3.2	The allocation of responsibilities among the central bank, the ministry of finance, or a separate public agency, for the primary debt issues, secondary market arrangements, depository facilities, and clearing and settlement arrangements for trade in government securities, should be publicly disclosed.
Description	In its function as banker to the government, SNB is acting as agent for the issuance of government bills and bonds (art. 14, para. 13 NBL). It also maintains the federal debt register (art. 15, para. 1 NBL) for recording bond issues by the federal government. Furthermore, the SNB acts as the main paying agent for government bills and bonds. The SNB does not perform other functions in the issue, deposition or clearing and settlement of government debt instruments.
Assessment	Observed.
Comments	The federal debt register will be abolished in the proposed revised NBL.
II. OPEN PROCESS FOR FORMULATING AND REPORTING MONETARY POLICY DECISIONS	
2.1	**The framework, instruments, and any targets that are used to pursue the objectives of monetary policy should be publicly disclosed and explained.**
Description	Switzerland has been operating under a floating exchange rate regime since the collapse of the Bretton Woods system in 1973, with an independent monetary policy geared towards price stability. However, the SNB retains the option to offset undesirable exchange rate developments, should it become necessary. In the past quarter century, the SNB conducted its monetary policy in a monetary targeting framework based, initially, on annual target growth rates of M1 and subsequently base money, and since 1990 on a medium-term (five-year) growth target on base money. As a number of velocity shifts made the relation between base money and price increasingly more tenuous, the SNB started to consider other indicators (e.g., M3) as supplementary indicators. Since 2000, monetary policy has been set on the strength of the inflation forecast over a three-year horizon with an explicit objective of keeping medium-term inflation below 2 percent, but not negative. To avoid destabilizing economic activity, the SNB refrains from fine-tuning inflation and is prepared to tolerate brief periods when headline inflation is outside the target range due to temporary factors that monetary policy can influence only to a limited extent. It reacts to such factors only if they pose a threat to medium-term price stability. The inflation forecast is a consensus forecast that blends a qualitative assessment of monetary and business cycle conditions and model-based forecasts of inflation under the assumption of unchanged interest rates. More importantly, the forecast is the official forecast of the SNB: this implies an institutional commitment to it and establishes a clear link between the inflation forecast and the instruments of monetary policy. At the operational level, the new framework entails a switch from internal targets on bank reserves to a publicly announced interest rate target in the form of a range for the three–month Swiss franc LIBOR. The monetary policy framework is effectively explained in SNB publications, including speeches of senior officials, and are posted on SNB's website. Monetary policy decisions that are taken by the Governing Board at its regular quarterly meetings are communicated in the "Monetary Policy Assessment," which presents the motivations underpinning the policy decision. A formal update of the inflation forecast and the underlying assumptions complements the "Monetary Policy Assessment." The Governing Board meets every week and can change the monetary policy stance at any meeting. If the policy is changed outside the regular quarterly cycle, a press communiqué is immediately issued.
Assessment	Observed.
Comments	The new monetary policy framework does not specify how the SNB is supposed to operate when medium-term inflation is in the range of price stability. However, it is generally understood that, when price stability is assured, the SNB pursues a monetary policy that depends on the prevailing economic conditions.

	The inflation forecast is based on the presumption of unchanged future interest rates. Although this is a reasonable assumption in a stable environment, in more volatile circumstances it may not be sustainable. In particular, an unchanged interest-rate inflation forecast that breaches the price stability range would signal an adjustment in the monetary policy stance. The SNB revises its published inflation forecast only in December and June. However, at its mid-semester monetary policy reviews and also when the monetary policy stance is adjusted outside the six-month cycle, the SNB provides a qualitative update of the inflation forecast. The implementation of this framework would benefit from greater transparency regarding the analytical underpinnings of the inflation forecast. In the past year, the SNB has made considerable progress in addressing this issue by publishing more detailed information about its analytical framework and the rationale for monetary policy decisions; but it has also made it clear that monetary policy decisions are not made in a mechanical way: they are based on models as well as on a qualitative assessment of economic conditions and prospects.
2.1.1	The procedures and practices governing monetary policy instruments and operations should be publicly disclosed and explained.
Description	In 1998, the SNB switched from foreign exchange swaps to short-term repos as the main instrument of steering liquidity. This followed a partial revision of the NBL in 1997 that allowed the SNB to conclude repo agreements. Since 2000, the SNB has been announcing (as an operational target) a target range of 100 basis points for the three–month Swiss franc LIBOR. Repo auctions are held on a daily basis. Information on repo procedures and practices is available on the websites of the SNB and the EurexRepo.
Assessment	Observed.
Comments	The switch in June 1999 from telephone to electronic trading increased market transparency and reduced spreads. Repos have an advantage over foreign exchange swaps as a monetary policy instrument because they make SNB liquidity directly accessible to smaller or foreign banks. Since the introduction of repo operations, the big banks have ceased to play a liquidity distributor role in the money market. The SNB may conclude repo agreements outside the daily auctions.
2.1.2	The rules and procedures for the central bank's relationships and transactions with counterparties in its monetary operations and in the markets where it operates should be publicly disclosed.
Description	All Swiss-based banks are eligible to participate in SNB's monetary policy repo operations. Banks domiciled abroad may also participate provided they fulfill certain criteria (essentially a minimum rating). Participating institutions are required to sign an agreement and need to have access to the electronic trading platforms of EurexRepo, SIS (SegaInterSettle), and SIC (Swiss Interbank Clearing). Information about the contracts and the terms and conditions is available upon request to interested parties. The Lombard facility (advances against securities) is available to all Switzerland-based banks that have signed an agreement and have deposited the collateral securities. The decision on the amount of the Lombard limit is based on the amount of collateral that banks can pledge. The basket of eligible securities is available on SNB's website. Counterparts for foreign exchange and reserve management transactions are chosen according to the quality of their services. The procedure is not publicly disclosed.
Assessment	The practice is broadly observed.
Comments	In 1999, the SNB discontinued foreign exchange swaps and access to the discount window. However, the principles for selecting counterparties in foreign exchange transactions with the SNB should be disclosed.

2.2	**Where a permanent monetary policy making body meets to assess underlying economic developments, monitor progress toward achieving its monetary policy objective(s), and formulate policy for the period ahead, information on the composition, structure, and functions of that body should be publicly disclosed.**
Description	Monetary policy decisions are taken by the Governing Board. Its composition, structure and functions are defined in the NBL (see 1.1.7 above). Decisions are consensus based.
Assessment	Observed.
Comments	The daily management of monetary policy is entrusted with SNB's Monetary Operations Division.
2.2.1	If the policy making body has regularly scheduled meetings to assess underlying economic developments, monitor progress toward achieving its monetary policy objective(s), and formulate policy for the period ahead, the advance meeting schedule should be publicly disclosed.
Description	Generally, the Governing Board meets every Thursday. In addition, the dates for the four meetings, at which the Governing Board takes a broad view of monetary policy, are pre-announced. Furthermore, the Government Board may meet on an ad hoc basis if needed.
Assessment	Observed.
Comments	Minutes of the Governing Board's meetings are not published. Meetings of the Governing Board are immediately followed by a press release whenever there is a change in policy.
2.3	**Changes in the setting of monetary policy instruments (other than fine-tuning measures) should be publicly announced and explained in a timely manner.**
Description	All changes in the setting of monetary policy instruments are explained and disclosed to the public through a press release, which is also posted at SNB's website.
Assessment	Observed.
Comments	The wide range (100 basis points) for the operational interest rate target allows some flexibility to accommodate liquidity or exchange rate shocks without signaling a change in the monetary policy stance. To reduce the ambiguity implied by the wide range, the SNB generally announces also a zone within the target range in which it expects the three-month Swiss franc LIBOR to fluctuate.
2.3.1	The central bank should publicly disclose, with a preannounced maximum delay, the main considerations underlying its monetary policy decisions.
Description	See 2.3 above.
Assessment	Observed.
Comments	
2.4	**The central bank should issue periodic public statements on progress toward achieving its monetary policy objective(s) as well as prospects for achieving them. The arrangements could differ depending on the monetary policy framework, including the exchange rate regime.**
Description	The main vehicle of the SNB's reporting to the public on progress toward achieving the monetary policy objectives is the quarterly "Monetary Policy Assessment," which is posted on SNB's website and published in its quarterly bulletin. The report includes an overview of macroeconomic developments and an informal update of its medium-term inflation forecast. A formal update of the inflation forecast is provided in the December and June issues of the "Monetary Policy Assessment." Outside the regular quarterly cycle, senior SNB management provide, through speeches and statements, updated assessments of macroeconomic developments and prospects.

Assessment	Observed.
Comments	The publication of a quarterly report will be institutionalized in the revised NBL (art. 7.4 revNBL).
2.4.1	The central bank should periodically present its monetary policy objectives to the public, specifying, inter alia, their rationale, quantitative targets and instruments where applicable, and the key underlying assumptions.
Description	See 2.4 above
Assessment	Observed.
Comments	The SNB gives no quantitative indication about the uncertainty surrounding its inflation forecast; it provides, however, a discussion of the risks in its "Monetary Policy Assessment" The main reason for not providing a quantitative indication of the risks is that the inflation forecast, as a consensus forecast, is not obtained by a single econometric model. See also section 2.1 above.
2.4.2	The central bank should present to the public on a specified schedule a report on the evolving macroeconomic situation, and their implications for its monetary policy objective(s).
Description	See 2.4 above.
Assessment	Observed.
Comments	In addition to the publications mentioned in section 2.4, the SNB started in 2001 publishing ad hoc studies explaining the analytical underpinnings of its inflation forecast.
2.5	**For proposed substantive technical changes to the structure of monetary regulations, there should be a presumption in favor of public consultations, within an appropriate period.**
Description	Technical changes in monetary regulations such as reserve requirements, eligibility of collateral for discount, auction procedures, qualifications and rules and procedures for counterparties with whom the SNB conducts open market operations do not require a public consultation process. Although, in practice, the tendency is to hold such a process. On the other hand, changes in the monetary instruments requiring modification of the legal framework require a formal consultation procedure (art. 147 Constitution). Interested institutions, parties, and organizations are normally invited to participate in the consultations, but as a matter of principle, consultations are open to the public. Usually, written comments are filed with the competent federal authority. The bill with explanatory notes (*Botschaft*) is submitted by the Federal Council to Parliament and is accompanied by a report summarizing suggestions and proposals.
Assessment	Observed.
Comments	
2.6	**The regulations on data reporting by financial institutions to the central bank for monetary policy purposes should be publicly disclosed.**
Description	The SNB is empowered to ask private and public bodies for information needed to monitor monetary conditions. The legal basis for data reporting by financial institutions is article 16k, para. 1 NBL, article 7 Banking Law and article 64 of the Law on Investment Funds. The forms and instructions on data reporting to the SNB are available upon request by interested parties. In case of noncompliance, the SNB may not impose fines but may mandate a special audit performed by the auditors. If infringements are ascertained, the auditors must notify the Federal Banking Commission for action (art. 16k, para. 2 NBL). In principle, the SNB may publish the data in aggregate form provided that it is impossible to infer figures for individual institutions from the published data. Nonetheless, there is an implicit agreement between the SNB and reporting banks that sensitive data (e.g., certain

	breakdowns by origin of the customer) may only be published with the prior explicit consent of the banks; written regulations on this issue do not exist.
Assessment	Observed.
Comments	The proposed revised NBL will broaden the scope of powers of the SNB regarding data provision and contains a penal provision (art. 21 revNBL). See also 1.1.2.
III. PUBLIC AVAILABILITY OF INFORMATION ON MONETARY POLICY	
3.1	**Presentations and releases of central bank data should meet the standards related to coverage, periodicity, timeliness of data and access by the public that are consistent with the International Monetary Fund's data dissemination standards.**
Description	Since May 18, 2001, Switzerland meets the specifications for the coverage, periodicity, and timeliness of the SDDS data, and for the dissemination of advance release calendars. The advance release schedule is posted in the website of the SNB.
Assessment	Observed.
Comments	Switzerland subscribed to the SDDS in 1996 and its country data page can be accessed through the IMF website.
3.2	**The central bank should publicly disclose its balance sheet on a preannounced schedule and, after a predetermined interval, publicly disclose selected information on its aggregate market transactions.**
Description	The summary balance sheet statement (*Ausweis*) as of the 10th, 20th and the last day of the month is issued on the following business day and is posted at SNB's website. These 10-day statements are very similar to the audited year-end balance sheet and they do not provide information on SNB's claims on general government (see 1.2.2 and 1.2.3 above). The Annual Report, which contains the audited year-end balance sheet and notes to the accounts, is made available to the public in April. The Monthly Statistical Bulletin provides monthly aggregated information on selected transactions.
Assessment	Observed.
Comments	
3.2.1	Summary central bank balance sheets should be publicly disclosed on a frequent and preannounced schedule. Detailed central bank balance sheets prepared according to appropriate and publicly documented accounting standards should be publicly disclosed at least annually by the central bank.
Description	See 3.2 above.
Assessment	Observed.
Comments	The SNB's financial statements are drawn up according to the Swiss Accounting and Reporting Recommendations. In addition, the SNB partially follows the international accounting standards (IAS and US-GAAP). It is desirable that the 10-day statements include information on claims on the general government.
3.2.2	Information on the central bank's monetary operations, including aggregate amounts and terms of refinance or other facilities (subject to the maintenance of commercial confidentiality) should be publicly disclosed on a preannounced schedule.
Description	The terms of the regular repo auctions (maturity and interest rate) are published daily at 9 a.m. on the main electronic information services (Reuters, Bloomberg, Telerate). The aggregate amount eventually allocated is not published. However, those having access to Eurex may form an opinion from the daily list of transactions. The outstanding balance of repos is published in the periodic summary statement of the SNB. Foreign exchange swaps have not been used as an instrument since 2000. If they were

	resumed, the reporting procedure would be similar to the one used for repos. The terms of the Lombard facility are published daily on the main electronic services. The outstanding balance of Lombard loans appears in the periodic summary statement of the SNB.
Assessment	Observed.
Comments	Disclosure of monetary operations is on a case-by-case basis. As a rule, the SNB does not release information on the volume of foreign exchange interventions. On the other hand, the SNB pre-announces a schedule with gold sales from its excess reserves.
3.2.3	Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by the central bank should be publicly disclosed through an appropriate central bank statement when such disclosure will not be disruptive to financial stability.
Description	There are no lender-of-last-resort provisions in the NBL and no specific rules for the disclosure of emergency financial support. Emergency financial support is provided through the Lombard or repo facility, the aggregate of which is disclosed in the periodic statement.
Assessment	The practice is broadly observed.
Comments	As a matter of principle, the SNB avoids commitment for liquidity support to prevent moral hazard. However, it would be advisable to establish internal rules on disclosure.
3.2.4	Information about the country's foreign exchange reserve assets, liabilities and commitments by the monetary authorities should be publicly disclosed on a preannounced schedule, consistent with the International Monetary Fund's Data Dissemination Standards.
Description	The data meet the specifications of the SDDS for the coverage, periodicity, and timeliness of the SDDS data (see also 3.1 above).
Assessment	Observed.
Comments	
3.3	**The central bank should establish and maintain public information services.**
Description	SNB's publications program includesan annual report (which is issued by April) and a quarterly and monthly bulletin. These are also posted at the SNB's website.
Assessment	Observed.
Comments	
3.3.1	The central bank should have a publications program, including an Annual Report.
Description	See 3.3.1 above.
Assessment	Observed.
Comments	
3.3.2	Senior central bank officials should be ready to explain their institution's objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.
Description	Senior officials of the SNB are ready to explain the SNB's objectives to the public and texts are available to the public. SNB senior officials may also appear before the Federal Government and selected parliamentary committees to explain the conduct of monetary policy and describe performance in achieving the objective of price stability. Views on macroeconomic developments and the financial system are also exchanged periodically with the Federal Finance Administration, the Federal Banking Commission, the State Secretariat for Economic Affairs, and commercial banks. There is a regular schedule for such appearances. For these meetings no written materials are circulated to the public.

Assessment	Observed.
Comments	
3.4	**Texts of regulations issued by the central bank should be readily available to the public.**
Description	The NBL empowers the SNB to issue ordinances (*Verordnungen*) only in connection with the measures mentioned in Article 16i, para 2 (ordinances have to be published in the Federal Gazette in order to become legally effective). However, it is generally recognized in legal doctrine that the SNB has the power, like the other federal agencies, to issue rules and regulations in discharging its statutory responsibilities, and thus it can issue ordinances even without a specific reference in its statute. The SNB has used this power several times in the past (e.g., Ordinance of 11th July 1979 on foreign bank deposits and foreign exchange future trades with foreigners). However, no such ordinances are currently in effect. Specific instructions to individual financial institutions are not published. Internal regulations are normally not published.
Assessment	Not applicable.
Comments	In the past twenty years, no specific instructions to financial institutions have been issued. Regarding the SNB's power to issue ordinances, the revised NBL will provide a more explicit basis (arts. 15, para. 3; 17 para. 5; 18 para.3 revNBL).
IV. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY THE CENTRAL BANK	
4.1	**Officials of the central bank should be available to appear before a designated public authority to report on the conduct of monetary policy, explain the policy objective(s) of their institution, describe their performance in achieving their objective(s), and, as appropriate, exchange views on the state of the economy and the financial system.**
Description	SNB's senior officials regularly appear before the federal government and selected parliamentary committees to explain the conduct of monetary policy, the policy objective of the SNB and to describe the performance in achieving the objective of price stability. The NBL provides for an exchange of views between the SNB and the federal government on economic and monetary policy decisions of major importance (art. 2, para. 5 NBL). The discussions focus on the state of the economy and the financial system. The SNB also exchanges views with the Federal Department of Finance, the State Secretariat for Economic Affairs, the Federal Banking Commission, the Swiss Banking Association, and large commercial banks. In order to inform the general public the SNB holds press conferences twice a year, which are well received.
Assessment	Observed.
Comments	The proposed revised NBL will provide for more specific rules on reporting. The SNB will discuss with the Federal Council the state of the economy, monetary and exchange rate policy and current issues on economic policy (art. 7, para. 1 revNBL). Both entities will inform each other before taking economic and monetary policy discussions of major importance (art. 7, para. 2 revNBL). The SNB will also inform the public on monetary and exchange rate policy and monetary intentions at least once a year (art. 7, para. 3 revNBL). In this context, it should be clarified that this information requirement foremost applies to reporting on past conduct. Policy intentions should be discussed in the context of the inflation forecast and not be specific regarding future actions.
4.2	**The central bank should publicly disclose audited financial statements of its operations on a preannounced schedule.**
Description	The law requires the publication of the annual accounts (art. 25, para. 3 NBL). The annual accounts must be approved by the Federal Council before publication and submission to the shareholders' meeting. The shareholders' meeting must approve the annual accounts by April

	of the following year at the latest (art. 37, para. 1 NBL). The audited financial statements of the SNB are included in the annual report, which is available to the public in April each year.
Assessment	Observed.
Comments	
4.2.1	The financial statements should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.
Description	As a public-law entity established in the legal form of a joint stock corporation, the SNB is mandated by law to have an independent audit. Each year the annual shareholders' meeting elects an auditing committee for this function (art. 51 NBL). The auditing committee comprises six persons, three certified accountants and three banking specialists. The auditing committee audits the annual accounts and balance sheet and reports to the shareholders' meeting. The auditing committee considers the work performed by an external audit firm (big five audit firm) and the internal auditors. In its accounting framework, the SNB applies the Swiss Accounting and Reporting Recommendations, but does not provide a cash flow statement or publish a mid-year statement. Balance sheet items are evaluated on a quarterly basis. There are some differing accounting methods used to reflect special features as Swiss central bank and note-issuing institution, which are explained in the notes to the accounts in the annual report.
Assessment	Observed.
Comments	Regarding auditing, the proposed revised NBL will clearly stipulate that the audit be carried out by an independent external auditor (arts. 44, 45 revNBL).
4.2.2	Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.
Description	The SNB has well-established internal governance procedures to control activities in the institution, such as on internal organization, governance, accounting and internal audit, computer usage, and avoidance of conflicts of interest. The documents are compiled in a staff handbook for internal use and are not publicly disclosed.
Assessment	Not observed.
Comments	It would be advisable to publish information on the integrity of operations, such as measures to address internal audit procedures.
4.3	**Information on the expenses and revenues in operating the central bank should be publicly disclosed annually.**
Description	Expenses and revenues are publicly disclosed in detail once a year in the annual report available to the public in April. Further details on the items in the income statement are provided in the notes to the income statement.
Assessment	Observed.
Comments	
4.4	**Standards for the conduct of personal financial affairs of officials and staff of the central bank and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.**
Description	Standards for the conduct of personal financial affairs for staff and officials (including members of the Governing Board) are set out in the general employment terms. Staff may carry out financial transactions for their own account at the premises of the SNB as long as they do not take up a lot of time and involve a reasonable proportion of assets. The use of confidential information and certain transactions such as day-trading, foreign exchange transactions or derivatives on foreign exchange rates or Swiss franc money-market rates are

	explicitly prohibited. Insider trading is an offense under article 161 of the Penal Code. Staff and officials must be prepared to disclose their financial transactions. For those individuals engaged in monetary operations, disclosure may be required to other banks upon request. Special permission by the Governing Board is required for officials or staff to engage in any other professional activity in order to limit potential conflicts of interest. Compliance with these rules is monitored by the internal audit, but the rules and regulations are not publicly disclosed.
Assessment	Not observed.
Comments	It would be advisable to publish information on standards for the conduct of personal financial affairs, such as measures to address conflicts of interest.
4.4.1	Information about legal protections for officials and staff of the central bank in the conduct of their official duties should be publicly disclosed.
Description	The officials and staff of the SNB are covered by federal legislation on civil or criminal liability (art. 59 NBL). Regarding civil liability, this provision is understood to refer to the Federal Law on the Liability of the Confederation, its Authorities and Officers. This statute governs the liability of an officer vis-à-vis the Confederation and vis-à-vis third party claimants. It provides protection to officers and staff and sets out clearly that third party claimants may only have a claim against the Confederation and not the individual officer or staff member (art. 3, para. 3 Liability Law). The Confederation may, however, take recourse against the officer or staff member in case of intentional or grossly negligent conduct. Criminal prosecution of federal officers is permitted only with the agreement of the Federal Department of Justice and Police (art. 15 Liability Law).
Assessment	Observed.
Comments	

Table 14. Summary Observance of IMF's MFP Transparency Code—Monetary Policy

Assessment Grade	Practices Grouped by Assessment Grade	
	Count	List
Observed	39	1.1, 1.1.1, 1.1.2, 1.1.3, 1.1.4, 1.1.5, 1.2, 1.2.1, 1.2.2, 1.2.3, 1.2.4, 1.2.5, 1.3, 1.3.1, 1.3.2 2.1, 2.1.1, 2.2, 2.2.1, 2.3, 2.3.1, 2.4, 2.4.1, 2.4.2, 2.5, 2.6 3.1, 3.2, 3.2.1, 3.2.2, 3.2.4, 3.3, 3.3.1, 3.3.2 4.1, 4.2, 4.2.1, 4.3, 4.4.1
Broadly observed	2	2.1.2, 3.2.3
Partly observed	1	1.1.7
Not observed	2	4.2.2, 4.4
Not applicable	2	1.1.6, 3.4

Recommended action plan and authorities' response to the assessment

Table 15. Recommended Action Plan—Monetary Policy Transparency

Reference Practice	Recommended Action
I. Clarity of Roles, Responsibilities and Objectives of Central Banks for Monetary Policy	It is recommended that the revised SNB law contain a provision explicitly requiring the publication of the annual report. It would be advisable to be more specific regarding the criteria to be applied to determine that a person no longer fulfills the conditions for exercising the duties as SNB's Governing Board member.
II. Open Process for Formulating and Reporting Monetary Policy Decisions	It is recommended that principles for selecting counterparties in foreign exchange transactions with the SNB be disclosed.
III. Public Availability of Information on Monetary Policy	It is desirable that the SNB discloses in its 10-day statements information on claims on general government. It would be advisable to establish internal rules for disclosing emergency liquidity support to banks.
IV. Accountability and Assurances of Integrity by the Central Bank	In the context of corporate governance, it would be advisable to publish information on the integrity of operations, such as measures to address conflicts of interest, and internal audit procedures.

Authorities' response

General remarks

The IMF's report on the compliance of the Swiss National Bank (SNB) and of Swiss monetary policy with the IMF Code of Good Practices on Transparency in Monetary and Financial Policies as part of the Financial Sector Assessment Program (FSAP) is of high quality. The analysis was conducted in a careful manner and contains some constructive criticism.

The SNB recognizes that the vast majority of practices are considered "observed," that is, they satisfy all essential criteria without significant deficiencies. From the report, it is also apparent that the new National Bank Law will strengthen the legal support of the transparency and the accountability efforts already undertaken by the SNB. Regarding monetary policy and the relation between the fiscal and monetary authorities, all practices are observed. In this very crucial area, the SNB complies comfortably with the high standards set by the IMF's code.

The report mentions two practices, which do not satisfy the essential criteria according to the IMF. The first practice refers to the prerequisites for board members and the criteria for the removal of board members. The IMF suggests setting clearer rules in this respect. Regarding this issue, the SNB intends to propose a corresponding clarification to be integrated in the new National Bank Law. The second point refers to the rules of internal governance and the conduct of personal financial affairs. With respect to this point, the SNB will review its standards to comply with the code.

The report addresses many important issues also in those practices, which were considered "observed." These points will be examined by the SNB and they may be helpful to improve further the transparency and accountability of monetary policy. In the remainder of the document, the SNB comments in detail on the actions recommended by the IMF.

Remarks on individual recommended actions

Practice 1.1.5

- Recommended action by the IMF: It is recommended that the proposed revised NBL should contain a provision explicitly requiring the publication of the annual report.
- Response by the SNB: The recommendation has been taken up. The draft of the revised NBL, which the Federal Council intends to submit to the Federal Assembly as a bill before the summer of 2002, will include an explicit provision requiring the publication of the annual report by the SNB (article 7, paragraph 4, rev. draft NBL).

Practice 1.1.7

- Recommended action by the IMF: It is recommended that the proposed revised NBL requires that SNB Board members be "fit and proper" individuals. Also, it would be advisable to be more specific regarding the criteria to be applied to determine that a person no longer fulfills the conditions for exercising the duties as SNB's Governing Board member.
- Response by the SNB: The suggestion to introduce a "fit and proper" requirement as a prerequisite for the election of members of the Governing Board or of the Bank Council was taken up; it will presumably be included in the bill to be submitted to the Federal Assembly. While the provision on the removal of members of the Governing Board will not be amended, the explicit reference to the prerequisites for election makes it clear that these are also relevant for a removal decision.

Practice 2.1.2

- Recommended action by the IMF: It is recommended to disclose principles for selecting counterparties in foreign exchange transactions with the SNB.
- Response by the SNB: As mentioned in the report, counterparties are chosen according to the quality of their services. This is the information the Swiss National Bank gives any potential counterparty requesting to do business with the SNB. The Swiss National Bank does not deem it necessary to publish additional details of the selection procedure.

Practice 3.2.1

- Recommended action by the IMF: It is desirable that the SNB discloses in its 10-day statements information on claims on general government.
- Response by the SNB: The SNB will examine the appropriateness of publishing information on holdings of government securities in the 10-day-statement.

Practice 3.2.3

- Recommended action by the IMF: It would be advisable to establish internal rules on disclosure.
- Response by the SNB: The SNB currently undertakes a review of its lender-of-last-resort function and will also address the question of establishing internal rules on disclosure regarding emergency financial support.

Practice 4.2.2 and practice 4.4

- Recommended action by the IMF: In the context of corporate governance, it would be advisable to publish information on the integrity of operations, such as measures to address conflicts of interest, and internal audit procedures.
- Response by the SNB: The rules on internal governance procedures and on the conduct of personal financial affairs will be subject to a comprehensive review in the course of the revision of the NBL. In this process, the SNB plans to carefully review its policy for the publication of internal rules and standards.

B. Transparency of Financial Policies—Banking and Securities

This section assesses the transparency of the arrangements for banking and securities regulation by the SFBC. The objective of the assessment was to measure Swiss banking supervision practice against the IMF Transparency Code.[8]

On the banking side, the assessment was based on the laws and regulations relating to banking supervision, particularly the Banking Act (BA), and the Banking Ordinance (BO). Reference was also made to circulars issued by the SFBC and by the SBA, which once approved by the SFBC are legally enforceable on all banks. The assessors read the SFBC's annual report, the annual report of the Swiss Banking Ombudsman, various press releases and other documentation released on the SFBC's website. The assessors had a series of conversations with the Director of the SFBC and his staff who had produced answers to a questionnaire provide by the mission. The assessors also met the Chairman of the SFBC. In addition, the assessors met with officials of the FFA, commercial banks supervised by the SFBC and external auditors who perform functions on behalf of the SFBC. The assessors also met staff of the Federal Reserve Bank of New York and the Financial Services Authority, who act as "host" supervisors for the large financial groups in New York and London.

On the securities side, the assessment was based on the laws and regulations relating to securities supervision. Reference was also made to circulars issued by the SFBC, by the Swiss Bankers Association (SBA) and by the Swiss Funds Association (SFA). The assessors read the SFBC's annual report, various press releases and other documentation released on the SFBC's website. The assessor had a series of conversations with the SFBC's staff that produced answers to a questionnaire provided by the mission. In addition, the assessors met representatives of supervised entities.

Practice-by-practice assessment

Table 16. Detailed Assessment of Observance of Transparency Code—Banking and Securities

V. Clarity of Roles, Responsibilities, and Objectives of Financial Agencies Responsible for Financial Policies	
5.1	**The broad objective(s) and institutional framework of financial agencies should be clearly defined, preferably in relevant legislation or regulation.**
Description	The Federal Banking Commission (SFBC) was established as banking regulator by the Federal Law on Banks and Saving banks (November 8, 1934 as subsequently amended). The Federal Act on Stock Exchanges and Securities Trading (March, 24, 1995 effective from 1997)

[8] The assessment was carried out by Peter Hayward (IMF), Nicoletta Giusto (CONSOB, Italy), Kathleen O'Brien (Office of the Comptroller of the Currency, US), and Stefan Spamer (Deutsche Bundesbank, Germany). It is based on information available during the FSAP mision in October 2001.

	regulates the jurisdiction of the SFBC in the securities field. According to these laws, the SFBC is responsible for licensing and supervision of banks, securities dealers and stock exchanges; disclosure of shareholdings in listed companies and take-over bids. Competences are shared with the SWX and the Takeover Board.
Assessment	Broadly observed.
Comments	The law is written in very broad terms leaving considerable flexibility to the SFBC, which, however, is careful to use it in a consistent and transparent fashion.
5.1.1	The broad objective(s) of financial agencies should be publicly disclosed and explained.
Description	The functions and organization of the SFBC are set out in Article 23 of the BA. The SFBC's objectives are explained in the annual report and other documents. The SFBC reports once a year to the Federal Council. The Federal Council and the Federal Department of Finance may require special reports. The SFBC communicates with the Federal Council via the Federal Department of Finance. The SFBC publishes bulletins on a periodic basis. It also maintains a website (http://www.ebk.admin.ch).
Assessment	Broadly observed.
Comments	While the task is clearly described in the law, neither the SFBC nor the legislature have set out the purpose of supervision nor the objectives of the agency. The Zufferey report on financial sector supervision in Switzerland recommended that the Banking Act should contain a statement of the principle objectives of supervision as a signal both to banks and to their customers as to the purposes of supervision. The report noted that the laws relating to securities and insurance supervision do that.
5.1.2	The responsibilities of the financial agencies and the authority to conduct financial policies should be publicly disclosed.
Description	Clearly described in Article 23 of the Banking Act.
Assessment	Observed.
Comments	The responsibility of the SFBC is clearly stated although there may be room for some clarification of the role of the Swiss Bankers' Association and that of banks' external auditors in the law.
5.1.3	Where applicable, the broad modalities of accountability for financial agencies should be publicly disclosed.
Description	The Director and his deputy are appointed by the Federal Council. The SFBC appoint the staff of the secretariat. The Banking Act also required the SFBC to furnish an annual report to the Federal Council and to the legislature. The Chairman and senior officials of the Commission are required to appear before Parliamentary committees when they discuss the report, although in plenary sessions, the Minster represents the Commission. Such accountability takes place on a strict post hoc basis (i.e., after the relevant events and the supervisory response have occurred and not while consideration of the issue is still under way). It is accepted that the Commission has sole authority in current cases before it, subject to appeal only to the Federal Supreme Court.
Assessment	Observed.
Comments	
5.1.4	Where applicable, the procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing bodies of financial agencies should be

	publicly disclosed.
Description	The Chairman and members of the commission as well as its Director and his deputy are appointed by the Federal Council for four year terms. The Federal Council has the power to remove these persons only in case of misdemeanors or serious abuse of their functions. This has happened only once during the SFBC's 65-year history.
Assessment	Observed.
Comments	
5.2	**The relationship between financial agencies should be publicly disclosed.**
Description	The SFBC is required to make its annual report to the Federal Finance Department. The Minister responsible for the department also introduces legislation and the Federal Council makes implementing ordinances. The Banking Act describes the relationship between the SFBC and the SNB. There are provisions for the exchange of information between them. The SNB collects the bulk of the banking statistics provided by supervised institutions and passes them to the SFBC for analysis. The relationship between the SFBC and the SWX or the Takeover Board is regulated by the Stock Exchange law and the relevant implementing legislation.
Assessment	Broadly observed.
Comments	Effectively the SFBC, a relatively small organization, contracts to the SNB its data processing requirements. This arrangement appears to function well. There is scope for formalizing the relationships between the SFBC, the FOPI, the SNB and the Federal Finance Administration by means of a memorandum of understanding. Arrangements between the SFBC and the FOPI for the supervision of conglomerates are not formally provided for in legislation but the informal arrangements have been made public.
5.3	**The role of oversight agencies with regard to payment systems should be publicly disclosed.**
Description	The SFBC does not supervise payment systems. This is done by the SNB (see separate assessment).
Assessment	Not applicable.
Comments	
5.3.1	The agencies overseeing payment systems should promote the timely public disclosure of general policy principles (including risk management policies) that affect the robustness of systemically important payment systems.
Description	See above.
Assessment	Not applicable.
Comments	
5.4	**Where financial agencies have oversight responsibilities for self-regulatory organizations (e.g., payment systems), the relationship between them should be publicly disclosed.**
Description	The SFBC has a close relationship with the Swiss Bankers' Association (SBA) and the Swiss Funds Association (SFA). The Associations' guidelines once approved by the SFBC are considered as a licensing requirement. External auditors are obliged to ensure compliance with the SBA and SFA guidelines and the SFBC can enforce them in the courts. These arrangements are well established. The SBA and SFA publish their guidelines and they are given publicity in the SFBC's publications.

Assessment	Observed.
Comments	The relationship with the SBA and SFA is stronger than in many other countries. Indeed the SBA's guidelines are enforced even on those few banks that are not members of the SBA.
5.5	**Where self-regulatory organizations are authorized to perform part of the regulatory and supervisory process, they should be guided by the same good transparency practices specified for financial agencies.**
Description	The SBA and SFA guidelines are normally enforced by the SFBC and are effectively therefore public law obligations. In one case, the "due diligence" agreement of 1977 which requires members to observe "know your customer" rules, members can be fined by the association for non-compliance. The SBA and SFA guidelines are published by the Associations. The SWX publishes its decisions and an annual report, and maintains a website where information is provided to the public. The Takeover Board maintains a website.
Assessment	Observed.
Comments	
VI. Open Process for Formulating and Reporting of Financial Policies	
6.1	**The conduct of policies by financial agencies should be transparent, compatible with confidentiality considerations and the need to preserve the effectiveness of actions by regulatory and oversight agencies.**
Description	The Banking Act and Ordinance contain the main supervisory requirements. These are supplemented by circulars. In addition the SFBC's annual report and quarterly bulletins describe actions and decisions taken by the SFBC and give statistics on the issue and withdrawal of licenses and other pertinent information.
Assessment	Observed.
Comments	Decisions affecting individual institutions are not normally published.
6.1.1	The regulatory framework and operating procedures governing the conduct of financial policies should be publicly disclosed and explained.
Description	See above.
Assessment	Observed.
Comments	
6.1.2	The regulations for financial reporting by financial institutions to financial agencies should be publicly disclosed.
Description	The law, ordinances, circulars, and decisions are all publicly available.
Assessment	Observed
Comments	
6.1.3	The regulations for the operation of organized financial markets (including those for issuers of traded financial instruments) should be publicly disclosed.
Description	The relevant rules are published by the SFBC, in the bulletin of the SWX and on its website.
Assessment	Observed.
Comments	

6.1.4	Where financial agencies charge fees to financial institutions, the structure of such fees should be publicly disclosed.
Description	The SFBC's fee structure is set out in regulations that is available, inter alia on the SFBC's website.
Assessment	Observed.
Comments	
6.1.5	Where applicable, formal procedures for information sharing and consultation between financial agencies (including central banks), domestic and international, should be publicly disclosed.
Description	Exchange of information is regulated by law. At the domestic level, the law regulates the relationship with the auditors, the SWX, the Takeover Board, and the SNB. The exchange of information with pension fund and insurance authorities it is not regulated. Particular restrictions are applicable when information on clients is concerned. Exchange of information with foreign counterparties is regulated by the law (Article 38 of the Federal Act on Stock Exchanges and Securities Trading). The law distinguishes two cases: information on supervised entities and information on clients of Swiss intermediaries. In the case of confidential information concerning clients the Federal Act on Administrative Procedure is applicable and, therefore, if the client does not consent, it will be up to the relevant Court to decide whether the information can be passed. The SFBC lists in its annual report the cooperation arrangements it has made with foreign banking supervisory agencies. It has been decided to publish the texts of such arrangements where the foreign agency has given its consent. In several important cases, the SFBC, and their foreign counterparts, have found no need to formalize the basis of their arrangements which perform to the satisfaction of both parties without formality.
Assessment	Broadly observed.
Comments	Given the fact that the two major banking groups have foreign business in excess of domestic business this aspect is particularly important. The importance is recognized in the SFBC's annual report.
6.2	**Significant changes in financial policies should be publicly announced and explained in a timely manner.**
Description	Changes of policy are announced by means of press notices that are also made available on the SFBC's website.
Assessment	Observed.
Comments	
6.3	**Financial agencies should issue periodic public reports on how their overall policy objectives are being pursued.**
Description	The SFBC issues a substantive annual report drawing attention to major developments in the financial system and major changes to its supervisory regime. The annual report is updated with quarterly bulletins. The SWX and Takeover Board also publish annual reports.
Assessment	Observed.
Comments	
6.4	**For proposed substantive technical changes to the structure of financial regulations, there should be a presumption in favor of public consultations, within an appropriate period.**

Description	Broad consultation with affected parties is undertaken for all significant legislative and other policy changes where time permits. In some cases a working group consisting of officials and representatives of the institutions affected is set up to prepare such changes. Normally, the SFBC endorses rules suggested by the relevant Trade Associations. The consultation process is not formalized in the legislation.
Assessment	Observed.
Comments	It is unclear to what extent end-investors and other market users participate in the consultation process or are heard before the formal adoption of new rules.
VII. PUBLIC AVAILABILITY OF INFORMATION ON FINANCIAL POLICIES	
7.1	**Financial agencies should issue a periodic public report on the major developments of the sector(s) of the financial system for which they carry designated responsibility.**
Description	As noted above, the SFBC publishes an annual report and quarterly bulletins in French and German. These are available on the SFBC's website, as are press releases and other material. The SWX and Takeover Board also publish annual reports.
Assessment	Observed.
Comments	
7.2	**Financial agencies should seek to ensure that, consistent with confidentiality requirements, there is public reporting of aggregate data related to their jurisdictional responsibilities on a timely and regular basis.**
Description	Financial statistics are published by the SNB. Data on the SFBC's activities, for example, licenses issued etc. is published in the SFBC's annual report
Assessment	Broadly observed.
Comments	The annual report does not contain statistics on the activities, for example, balance sheet developments and profitability, of the institutions it supervises. These are however, available elsewhere.
7.3	**Where applicable, financial agencies should publicly disclose their balance sheets on a preannounced schedule and, after a predetermined interval, publicly disclose information on aggregate market transactions.**
Description	The annual report contains an account of the SFBC's income and expenditure, but not its balance sheet, for the year. The basis for its income is laid down in an ordinance that prescribes the fees for supervision and the SFBC's other activities.
Assessment	Broadly observed.
Comments	
7.3.1	Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by financial agencies should be publicly disclosed through an appropriate statement when such disclosure will not be disruptive to financial stability.
Description	The SFBC is not a financial institution and therefore does not possess the resources to provide any financial assistance nor does it have powers to do so
Assessment	Not applicable.
Comments	The SNB would be the appropriate agency for any such assistance.

7.4	**Financial agencies should establish and maintain public information services.**
Description	The agency has pursued a policy of being open to the press and other inquirers and publishes extensively. The SFBC, the SWX and the Takeover Board maintain websites. Information is also available on request in paper form.
Assessment	Observed.
Comments	In view of the public interest in its activities, the SFBC now has a full time press officer.
7.4.1	Financial agencies should have a publications program, including a periodic public report on their principal activities issued at least annually.
Description	As noted above, the SFBC, SWX and Takeover Board publish annual reports. The SFBC also issues quarterly bulletins and makes periodic press releases.
Assessment	Observed.
Comments	
7.4.2	Senior financial agency officials should be ready to explain their institution's objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.
Description	Senior officials of the SFBC make periodic presentations to the Parliament and are available to the press as a matter of policy.
Assessment	Observed.
Comments	
7.5	**Texts of regulations and any other generally applicable directives and guidelines issued by financial agencies should be readily available to the public.**
Description	All generally applicable directives and guidelines are published and made available on the websites of the SFBC, SWX, and Takeover Board.
Assessment	Observed.
Comments	The SFBC does not normally publish decisions affecting individual institutions unless there is a perceived public interest in its doing so.
7.6	**Where there are deposit insurance guarantees, policyholder guarantees, and any other client asset protection schemes, information on the nature and form of such protections, the operating procedures, how the guarantee is financed, and the performance of the arrangement should be publicly disclosed.**
Description	At present the Swiss deposit protection scheme is a voluntary one and is managed by the Swiss Bankers' Association. The agreement among the members of the SBA is a public document available on the SBA's website. The scheme is an ex-post scheme and hence there is no fund and no accounts to be prepared. The scheme has only been activated once (in 1991) and no problem arose with its operation.
Assessment	Observed.
Comments	It is intended that the present scheme be replaced by a compulsory scheme based on a statutory provision but still managed by the SBA.
7.7	**Where financial agencies oversee consumer protection arrangements (such as dispute settlement processes), information on such arrangements should be publicly disclosed.**
Description	Disputes between banks and their customers are subject to the ombudsman scheme. The

	ombudsman issues an annual report that gives details of complaints made and their treatment. Where complaints are made to the SFBC, the Commission will examine the complaint with a view to determining whether they reflect any violation of the banking act or possible organizational shortcomings. Individual cases will be referred to the ombudsman.
Assessment	Observed.
Comments	
VIII. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY FINANCIAL AGENCIES	
8.1	**Officials of financial agencies should be available to appear before a designated public authority to report on the conduct of financial policies, explain the policy objective(s) of their institution, describe their performance in pursuing their objective(s), and, as appropriate, exchange views on the state of the financial system.**
Description	The Chairman and the Director of the SFBC appear regularly before Parliamentary Committees to explain the operations of the SFBC following publication of the annual report. Accountability before the plenary Parliament is normally by the Minister of Finance who is answerable to Parliament and is responsible for presenting legislation on banking supervision.
Assessment	Observed.
Comments	
8.2	**Where applicable, financial agencies should publicly disclose audited financial statements of their operations on a pre-announced schedule.**
Description	A simple income and expenditure statement is included in the SFBC's annual report. The SFBC is considered a part of the government for financial purposes. It has no independent financial existence and therefore is not responsible for accounting. This is the responsibility of the FFA. The financing of the SFBC is subject to the same auditing arrangements as apply to the FFA.
Assessment	Not applicable.
Comments	As noted above, the SFBC is not a financial institution and its efficacy and the transparency of its activities are not dependent on the publication of audited financial statements.
8.2.1	Financial statements, if any, should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.
Description	The SFBC is subject to the normal audit arrangements of government agencies. As noted above, the SFBC is not a financial institution that holds assets and has liabilities to the public.
Assessment	Not applicable.
Comments	
8.2.2	Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.
Description	As stated above, the SFBC is subject to central government financial controls.
Assessment	Broadly observed.
Comments	
8.3	**Where applicable, information on the operating expenses and revenues of financial agencies should be publicly disclosed annually.**
Description	The expenses and revenues of the SFBC are disclosed in its annual report.

Assessment	Observed.
Comments	
8.4	**Standards for the conduct of personal financial affairs of officials and staff of financial agencies and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.**
Description	The SFBC has adopted an internal code of conduct concerning staff fiduciary obligations and personal transactions, which is published. Staff of the SFBC are subject to published guidelines which forbid the holding of securities issued by supervised institutions and carrying out any transactions based on information obtained in the course of their duties.
Assessment	Observed.
Comments	
8.4.1	Information about legal protections for officials and staff of financial agencies in the conduct of their official duties should be publicly disclosed.
Description	Rules on the legal protection for SFBC officials are publicly disclosed. SFBC staff may only be subject to criminal prosecution with the approval of the Federal Department of Justice and Police in order to ensure that civil servants are protected from unsubstantiated claims of alleged criminal behavior. A civil suit may not be brought against a member of the SFBC or its staff. Instead suit has to be brought against the confederation. Recourse can only be brought against the staff member if he or she has caused damage intentionally or by gross negligence.
Assessment	Observed.
Comments	

Table 17. Summary Observance of Transparency Code—Banking and Securities

Assessment Grade	Practices Grouped by Assessment Grade	
	Count	List
Observed	24	5.1.2, 5.1.3, 5.1.4, 5.4, 5.5, 6.1, 6.1.1, 6.1.2, 6.1.3, 6.1.4, 6.2, 6.3, 6.4, 7.1, 7.4, 7.4.1, 7.4.2, 7.5, 7.6, 7.7, 8.1, 8.3, 8.4, 8.4.1
Broadly observed	7	5.1, 5.1.1, 5.2, 6.1.5, 7.2, 7.3, 8.2.2
Partly observed		
Non-observed		
Not applicable	5	5.3, 5.3.1, 7.3.1, 8.2, 8.2.1

Recommended action plan and authorities' response to the assessment

Table 18. Recommended Action Plan— Banking and Securities Policies Transparency

Reference Practice	Recommended Action
BANKING AND SECURITIES	
V. Clarity of Roles, Responsibilities,	As noted in the Zufferey report, it would be helpful if the SFBC's

Reference Practice	Recommended Action
and Objectives of Financial Agencies Responsible for Financial Policies	objectives could be enshrined in the Banking Act when it is next revised. There may be scope for formalizing the relationships between the SFBC, the FOPI, the SNB and the Federal Finance Administration.

Authorities' response

The authorities were in agreement with the assessments.

C. Transparency of Financial Policies—Insurance

This assessment was performed using the IMF MFP Code of Good Practices on Transparency in Monetary and Financial Policies Methodology document that was adopted by the Executive Board on July 24, 2000.[9]

The assessment was based on a review of the following documents: (1) The self assessment prepared by the FOPI; (2) The relevant legislation, decrees and ordinances; and (3) Publications issued by the FOPI.

Practice-by-practice assessment

Table 19. Detailed Assessment of Observance of Transparency Code—Insurance

V. Clarity of Roles, Responsibilities, and Objectives of Financial Agencies Responsible for Financial Policies	
5.1	**The broad objective(s) and institutional framework of financial agencies should be clearly defined, preferably in relevant legislation or regulation.**
Description	Objectives are defined in the law on supervision of insurance companies at articles 1, 17 and 18. Institutional framework is defined in a special ordinance # 172.213.1.
Assessment	Observed.
Comments	The objective is to supervise insurance companies in order to protect the interests of their policyholders.
5.1.1	The broad objective(s) of financial agencies should be publicly disclosed and explained.
Description	All legislation, ordinances, and decrees are published. There is an official gazette "*Recueil Officiel des Lois Federales*" and most documents appear on the website. The FOPI also publishes a summary of significant developments in a section of a special insurance review published by a private sector group every six months.
Assessment	Observed.
Comments	Although the publication of the semi-annual revues has been interrupted, it will be resumed in the near future.
5.1.2	The responsibilities of the financial agencies and the authority to conduct financial policies should be publicly disclosed.
Description	The FOPI's responsibilities in the area of insurance supervision are made clear through the legislation and other publications. It has complete responsibility for the development of financial policies relative to insurance. This is made plain through its publications, its contact with the insurance trade association and the individual companies, and because it has a policy of broad distribution of draft policy documents for review and comment.
Assessment	Observed.
Comments	Although the FOPI is lodged for administrative purposes in the Ministry of Justice and Police

[9] The main author of this assessment is Donald McIsaac (World Bank).

	and Police, it has autonomy in the development of financial policies.
5.1.3	Where applicable, the broad modalities of accountability for financial agencies should be publicly disclosed.
Description	The FOPI has full accountability under the Swiss Constitution, laws and regulations. There is a special law on supervision of insurance companies as well as an ordinance governing the means of financing the office and calling for a budget.
Assessment	Observed.
Comments	
5.1.4	Where applicable, the procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing bodies of financial agencies should be publicly disclosed.
Description	Procedures for appointment and the terms of office for all FOPI staff, including its head, are defined by the Swiss laws for public servants. The director and the deputy director of the FOPI are appointed by and at the sufferance of the Federal Council acting within its prerogatives under the Swiss Constitution. These two, other members of FOPI staff, as for all Swiss public servants, have a contract, and in their case it provides for a four-year term (this will shortly be changed to an indefinite period).
Assessment	Observed.
Comments	
5.2	**The relationship between financial agencies should be publicly disclosed.**
Description	There are no formal relationships between financial agencies. A key, largely informal working relationship exists between the FOPI and the SFBC. A FOPI decree, in a conglomerate supervision case involving Zürich Financial Services illustrates the relationship. This is available on the Internet and will be published in the Swiss Insurance Review. There is also an informal working relationship with the Federal Office of Social Insurance. While the FOSI has primary responsibility for private pension funds and health insurance funds, some of these responsibilities are discharged by the FOPI.
Assessment	Broadly observed.
Comments	Work done by the FOPI in respect of pensions and health funds is disclosed to the foundations and the funds concerned. In addition, the FOPI's annual statistics report provides information on sickness funds as well as on insurance company activities.
5.3	**The role of oversight agencies with regard to payment systems should be publicly disclosed.**
Description	The FOPI has no role with respect to the payment system.
Assessment	Not applicable.
Comments	
5.3.1	The agencies overseeing the payment system should promote the timely public disclosure of general policy principles (including risk management policies) that affect the robustness of systemically important payment systems.
Description	
Assessment	Not applicable.
Comments	

5.4	**Where financial agencies have oversight responsibilities for self-regulatory organizations (e.g., payment systems), the relationship between them should be publicly disclosed.**
Description	An SRO (the *Organisme de l'Autoregulation de l'Association Suisse d'Assurances pour la Lutte contre le Blanchiment d'Argent, OA-ASA*) has been organized in collaboration with the Swiss Insurance Association, to assist with the monitoring of the Ant-Money Laundering efforts of Swiss insurance companies. The FOPI is responsible for supervising the operations of the SRO. This arrangement and the reporting relationships are disclosed through published reports of the Swiss Insurance Association and the SRO. The FOPI communicates directly with the SRO, the Money Laundering Report Office and with those companies that are not members of the SRO.
Assessment	Observed.
Comments	The FOPI is contemplating a new decree to extend the application of the AML rules to embrace all insurance companies. All such decrees are made public through direct distribution to the companies concerned and through the Internet.
5.5	**Where self-regulatory organizations are authorized to perform part of the regulatory and supervisory process, they should be guided by the same good transparency practices specified for financial agencies.**
Description	The SRO that has been organized with the support of the FOPI and the industry trade association provides an annual report on the results achieved by its members to the MLRO. Reports of the latter organization are made public although common sense dictates that not all information can be publicly disclosed.
Assessment	Observed.
Comments	
VI. OPEN PROCESS FOR FORMULATING AND REPORTING OF FINANCIAL POLICIES	
6.1	**The conduct of policies by financial agencies should be transparent, compatible with confidentiality considerations and the need to preserve the effectiveness of actions by regulatory and oversight agencies.**
Description	FOPI's supervisory activities involve a considerable reliance on the work of external auditors and company actuaries. FOPI's instructions to companies and their reporting professionals are supplied to the parties concerned but also made available to the general public through the Internet. Much of the data collected by the FOPI is published in an annual report, although some information such as solvency margin results is kept confidential.
Assessment	Observed.
Comments	The FOPI maintains a steady dialogue with industry players in the formulation and application of supervisory policy.
6.1.1	The regulatory framework and operating procedures governing the conduct of financial policies should be publicly disclosed and explained.
Description	These are disclosed in FOPI Information sheets and these are available to the public.
Assessment	Observed.
Comments	There are many such information sheets or circulars including some that embody sample forms for reporting to the FOPI. The documents are made available in all the official languages of Switzerland. At present, the FOPI does not apply a "fit and proper" screen to owners and managers of insurance companies that have or are seeking licenses. This will be contemplated in the future and it is hoped that the criteria used in making the assessment will be disclosed.

6.1.2	The regulations for financial reporting by financial institutions to financial agencies should be publicly disclosed.
Description	Insurance companies report their financial results to the FOPI using reporting forms that have been prescribed by the FOPI. The presentation is the same as that used in the European Union. The FOPI distributes instructions and draft forms to the companies. In their published accounts for the use of shareholders, companies will use a variety of approaches to financial reporting (US GAAP), IAS, and other pertinent standards. However the financial reports sent to the FOPI must be accompanied by a reconciliation of any differences between the statutory reports and the published ones.
Assessment	Observed.
Comments	
6.1.3	The regulations for the operation of organized financial markets (including those for issuers of traded financial instruments) should be publicly disclosed.
Description	
Assessment	Not applicable.
Comments	
6.1.4	Where financial agencies charge fees to financial institutions, the structure of such fees should be publicly disclosed.
Description	FOPI's expenses are recovered through a levy placed on the companies. The means of determining the fees is specified in an Ordinance. Each year the FOPI publishes an Information Sheet that specifies for each company the total amount of fees that will be charged and then indicates the proportion to be paid by the particular company. (Proportion is based on market share).
Assessment	Observed.
Comments	Because companies are advised of the total amount, they are in a position to determine whether their portion appears reasonable
6.1.5	Where applicable, formal procedures for information-sharing and consultation between financial agencies (including central banks), domestic and international, should be publicly disclosed.
Description	Based on general confidentiality rules applicable to public servants, and since the insurance laws do not provide any grounds for exception, the FOPI regards all the information that it collects as confidential and it cannot be shared. Over time, they have developed a pattern of making a substantial amount of data on company results available to the public. However, important items such as solvency margin information is not divulged. There are certain agreements that cover relations with financial sector supervisors in other jurisdictions - EU, Liechtenstein. However sharing of information with these other supervisors is restricted to information that is already in the public domain, such as the insurance company statistical data that appears in the annual report of the Office. Special decrees are in place or are contemplated that will broaden the capacity of the FOPI to share information. These decrees are issued with the consent of the conglomerate concerned and will authorize the sharing of all information with supervisors in other countries or in other financial sectors, such as banking. These decrees will appear on the Internet and also in a published review.
Assessment	Observed.
Comments	New legislation soon to be introduced will likely broaden the capacity of the FOPI to share

	information with other supervisors.
6.2	**Significant changes in financial policies should be publicly announced and explained in a timely manner.**
Description	The FOPI follows a practice of extensive consultation with the industry and affected parties prior to making any changes in policy. Changes are communicated through circular letters and the Internet.
Assessment	Observed.
Comments	Working committees of the trade association are established to work with the FOPI in the development of new laws, regulations, guidelines, etc.
6.3	**Financial agencies should issue periodic public reports on how their overall policy objectives are being pursued.**
Description	The FOPI does not issue a regular report that discusses the pursuit of its policy objectives.
Assessment	Not observed.
Comments	The annual statistical report could be enhanced if a section was added to the report in which the FOPI described its objectives and indicated what progress is being made in achieving those objectives.
6.4	**For proposed substantive technical changes to the structure of financial regulations, there should be a presumption in favor of public consultations, within an appropriate period.**
Description	Draft copies of proposed changes to regulations, legislation, etc. are circulated to affected industry players for comment. There are often joint industry/government working groups to analyze specific topics. Consultation is mandatory by virtue of article 42 of the insurance supervisory law.
Assessment	Observed.
Comments	Draft material is also circulated by Internet as well as by circular letter
VII. PUBLIC AVAILABILITY OF INFORMATION ON FINANCIAL POLICIES	
7.1	**Financial agencies should issue a periodic public report on the major developments of the sector(s) of the financial system for which they carry designated responsibility.**
Description	The Annual report is primarily statistical in nature. However it does provide a vehicle for comments on major developments.
Assessment	Broadly observed.
Comments	Issues concerning emerging risks could be addressed in the report.
7.2	**Financial agencies should seek to ensure that, consistent with confidentiality requirements, there is public reporting of aggregate data related to their jurisdictional responsibilities on a timely and regular basis.**
Description	Aggregate data are available through the annual report.
Assessment	Observed.
Comments	Additional information is made available through the website.
7.3	**Where applicable, financial agencies should publicly disclose their balance sheets on a preannounced schedule and, after a predetermined interval, publicly disclose information on aggregate market transactions.**

Description	The FOPI prepares a report on its receipts and expenditures and this appears as a section in the government accounts. The details of expenditures are provided in the annual notice regarding fees to be paid by companies. There is no balance sheet as all revenues are remitted to the Treasury, which supplies the resources that the FOPI needs. The FOPI does not engage in market transactions.
Assessment	Broadly observed.
Comments	
7.3.1	Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by financial agencies should be publicly disclosed through an appropriate statement when such disclosure will not be disruptive to financial stability.
Description	The FOPI does not provide emergency financial support.
Assessment	Not applicable.
Comments	
7.4	**Financial agencies should establish and maintain public information services.**
Description	The FOPI has appointed an Information Officer who manages the information function for the authority within and in collaboration with other officers in the Central Services section of the FOPI.
Assessment	Observed.
Comments	
7.4.1	Financial agencies should have a publications program, including a periodic public report on their principal activities issued at least annually.
Description	The annual report has been described previously.
Assessment	Broadly observed.
Comments	The report does not describe all the activities performed by the FOPI although it does provide information concerning new licenses granted.
7.4.2	Senior financial agency officials should be ready to explain their institution's objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.
Description	Appearances and other information instruments are used by senior staff as required. The head of the FOPI is called to testify before a parliamentary committee at least once per year to discuss the program. Head and other members of senior staff represent the FOPI at industry and public conferences.
Assessment	Observed.
Comments	
7.5	**Texts of regulations and any other generally applicable directives and guidelines issued by financial agencies should be readily available to the public.**
Description	All texts are made available in print form to the affected companies and through the *Receuil Officiel*. Documents are also made generally available through the Internet.
Assessment	Observed.

Comments	
7.6	**Where there are deposit insurance guarantees, policyholder guarantees, and any other client asset protection schemes, information on the nature and form of such protections, on the operating procedures, on how the guarantee is financed, and on the performance of the arrangement, should be publicly disclosed.**
Description	There are no deposit insurance-type schemes provided for insurance policyholders in Switzerland.
Assessment	Not applicable.
Comments	
7.7	**Where financial agencies oversee consumer protection arrangements (such as dispute settlement processes), information on such arrangements should be publicly disclosed.**
Description	The FOPI will respond to complaints and inquiries to the extent possible. However the insurance industry has an ombudsman who is better positioned to respond to such inquiries.
Assessment	Broadly observed.
Comments	The FOPI should perhaps establish an identified section of its website for the receipt of consumer complaints.
VIII. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY FINANCIAL AGENCIES	
8.1	**Officials of financial agencies should be available to appear before a designated public authority to report on the conduct of financial policies, explain the policy objective(s) of their institution, describe their performance in pursuing their objective(s), and, as appropriate, exchange views on the state of the financial system.**
Description	See response to question 7.4.2.
Assessment	Observed.
Comments	
8.2	**Where applicable, financial agencies should publicly disclose audited financial statements of their operations on a preannounced schedule.**
Description	The FOPI does not produce audited financial statements. However it is subject to audit of its activities by the government auditors. Its results appear in the National Accounts once a year.
Assessment	Not applicable.
Comments	
8.2.1	Financial statements, if any, should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.
Description	
Assessment	Not applicable.
Comments	
8.2.2	Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.
Description	Internal governance procedures are based on the organizational Ordinance.

Assessment	Broadly observed.
Comments	The "*Ordonnance sur l'Organisation du Departement Fédéral de Justice et Police*" is a public document. It describes the functions and responsibilities of each unit within the Department, one of which is, of course, the Federal Office of Private Insurance. The main Department has a General Secretariat which is responsible for planning, coordination and control. The Secretariat also has a supervisory responsibility in respect of the activities of each "office" within the Department.
8.3	**Where applicable, information on the operating expenses and revenues of financial agencies should be publicly disclosed annually.**
Description	Swiss national accounts disclose this information. Expenditures are also disclosed in the notices sent to each company along with the request for annual fees.
Assessment	Observed.
Comments	
8.4	**Standards for the conduct of personal financial affairs of officials and staff of financial agencies and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.**
Description	Standards applied are those specified for all public servants by the General Public Service rules. These are explained to each employee at the time of hiring. The standards are publicly disclosed with other documents relating to public service employment.
Assessment	Observed.
Comments	
8.4.1	Information about legal protection for officials and staff of financial agencies in the conduct of their official duties should be publicly disclosed.
Description	There are no specific legal protections. However, under prevailing law, no action can be brought against a public servant in his personal capacity for actions performed in the course of the individual's regular duties. Any such action must be launched against the government. Disclosure with other government documents.
Assessment	Observed.
Comments	

Table 20. Summary Observance of Transparency Code—Insurance

Assessment Grade	Practices Grouped by Assessment Grade	
	Count	List
Observed	22	5.1, 5.1.1, 5.1.2, 5.1.3, 5.1.4, 5.4, 5.5, 6.1, 6.1.1, 6.1.2, 6.1.4, 6.1.5, 6.2, 6.4, 7.2, 7.4, 7.4.2, 7.5, 8.1, 8.3, 8.4, 8.4.1
Broadly observed	6	5.2, 7.1, 7.3, 7.4.1, 7.7, 8.2.2
Partly observed		
Non-observed	1	6.3
Not applicable	7	5.3, 5.3.1,6.1.3, 7.3.1, 7.6, 8.2, 8.2.1

Recommended action plan and authorities' response to the assessment

Table 21. Recommended Action Plan—Insurance Policies Transparency

Reference Practice	Recommended Action
INSURANCE	
V. Open Process for Formulating and Reporting of Financial Policies	The FOPI should consider including in its published annual report a discussion of its policy objectives and its achievements in meeting those objectives.
VI. Public Availability of Information on Financial Policies	The FOPI's annual report could also include a discussion concerning emerging risks, as well as a summary of FOPI's principal activities.

Authorities' response

The authorities were in agreement with the assessments.

D. Transparency of Financial Policies—Pensions

This section presents a discussion and assessment of practices in Switzerland regarding transparency in financial policies, with a focus on pension fund regulators, vis-à-vis the practices in the Code. The assessment of observance of each practice is made on a qualitative basis using a five-part assessment system: observed; broadly observed, partly observed; non-observed and not applicable.[10]

Supervisory roles and responsibilities in the pension system cut across agencies at the federal as well as cantonal level. The cantonal authorities designate supervisory authorities—the Cantonal Offices for Occupational Benefits Plans—to control the funds within the borders of the individual cantons.[11] Pension funds and social security institutions operating at the national or international level are supervised by the Federal Office of Social Insurance (FOSI). The law has also created an advisory Federal Commission on Occupational Benefits Plans with representatives from federal and cantonal governments, employers, employees, and the pension funds.

Practice-by-practice assessment

Table 22. Detailed Assessment of Observance of Transparency Code—Pensions

V. Clarity of Roles, Responsibilities and Objectives of Financial Agencies Responsible for Financial Policies	
5.1	**The broad objective(s) and institutional framework of financial agencies should be clearly defined, preferably in relevant legislation or regulation.**
Description	The institutional framework governing the roles, responsibilities and objectives of the financial agencies in charge of pension supervision and regulation are clearly defined in various pieces of legislation and regulation: the 1982 Law on Occupational Benefit Plans Concerning Old-age, Survivors and Invalidity (LPP); the 1983 Circular on the Supervision and Registration of Occupational Benefit Plans (BBV1); the 1984 Circular on Occupational Benefit Plans Concerning Old-age, Survivors and Invalidity (BBV2); the 1998 Circular on the Guarantee Fund (SFV1); the 1985 Regulation on the Organization of the Guarantee Fund (SFV2); and the 1984 Circular on Establishing Endowments for the Supervision of Occupational Benefit Plans (VGBV). These pieces of legislation and regulation are published in the official bulletin and disseminated through a variety of means, including the official websites of the FOSI, the Cantonal Offices, and the Confederation.
Assessment	Observed.
Comment	The Cantonal Offices for Occupational Benefits Plans have responsibility for supervision pension funds within the borders of the individual cantons. The FOSI has responsibility for supervision of pension funds operating at the national or international level, and of the Suppletory Fund (a foundation to which all employers who fail to establish a separate pension

[10] The main author of this assessment is Marina Moretti (IMF).

[11] With 15 professional staff, the Zürich Cantonal Office for Municipalities and Occupational Benefits Plans is the largest of such supervisory agencies.

	scheme are automatically affiliated). The FOSI, under the authority of the Federal Council, has also responsibility for "high surveillance," that is, oversight of the Cantonal Offices (LPP, Article 64). The FOSI is working on a project of revision to the law that would strengthen its "high surveillance" role as well as its role in the direct supervision of pension funds. Federal law applies to the regulation of pension funds.
5.1.1	The broad objective(s) of financial agencies should be publicly disclosed and explained.
Description	The objectives of pension regulatory agencies are not explicitly disclosed in the law, but are discussed in the various publications of the FOSI and the Cantonal Offices.
Assessment	Broadly observed.
Comment	Pension supervisors' main objectives are to oversee the protection of client assets and contribute to financial stability.
5.1.2	The responsibilities of the financial agencies and the authority to conduct financial policies should be publicly disclosed.
Description	The LPP (Article 62) empowers the FOSI and Cantonal Offices to (1) verify the conformity of regulations pertaining to pension funds with the law; (2) request periodical reporting of their activities from pension funds; (3) take knowledge of the reports prepared by the organs of internal control and the recognized expert (actuary); and (4) take the necessary measures to correct deficiencies.
Assessment	Observed.
Comment	
5.1.3	Where applicable, the broad modalities of accountability for financial agencies should be publicly disclosed.
Description	The Public Organizations Law prescribes all federal and cantonal organizations to publish an annual report. The FOSI annual report contains a discussion of regulatory changes and financial statistics of the pension system, as well as a brief overview of supervisory actions. The annual report is published every year with a two-year delay.
Assessment	Observed.
Comment	It would be advisable that the FOSI annual report be published in a more timely fashion. Accountability to the general public is limited by the lack of disclosure of supervisory agencies' financial statements (see 7.3 and 8.2 below).
5.1.4	Where applicable, the procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing bodies of financial agencies should be publicly disclosed.
Description	The rules on the appointment of the head of the supervisory agencies are established by law, and apply to all civil servants. The Director and the Deputy Director are appointed by the Federal Council acting within its prerogatives under the Swiss Constitution. These two, other staff of the FOSI, as for all Swiss public servants, have a contract, and in their case it provides for a four-year term (to be changed shortly to an indefinite period).
Assessment	Observed.
Comment	
5.2	**The relationship between financial agencies should be publicly disclosed.**
Description	Coordination among pension supervisors (cantonal and federal) is guaranteed by the "high surveillance" role of the FOSI (LPP Article 64).

	With regard to coordination with other financial agencies, the law has created an advisory Federal Commission on Occupational Benefits Plans with representatives from federal and cantonal governments, employers, employees, and the pension funds.
Assessment	Observed.
Comment	A "Conference" of Cantonal Offices facilitates the interaction between the cantonal and federal pension supervisory authorities, and there are periodical meetings on policy and technical issues. There are no separate inter-institutional agreements between the FOSI and other agencies, but in practice the FOSI consults other financial agencies—in particular, the insurance regulators—when drafting new legislation.
5.3	**The role of oversight agencies with regard to payment systems should be publicly disclosed.**
Description	
Assessment	Not applicable.
Comment	
5.4	**Where financial agencies have oversight responsibilities for self-regulatory organizations (e.g., payment systems), the relationship between them should be publicly disclosed.**
Description	
Assessment	Not applicable.
Comment	
5.5	**Where self-regulatory organizations are authorized to perform part of the regulatory and supervisory process, they should be guided by the same good transparency practices specified for financial agencies.**
Description	
Assessment	Not applicable.
Comment	
VI. OPEN PROCESS FOR FORMULATING AND REPORTING FINANCIAL POLICIES	
6.1	**The conduct of policies by financial agencies should be transparent, compatible with confidentiality considerations and the need to preserve the effectiveness of actions by regulatory and oversight agencies.**
Description	Overall, the conduct of policies by financial agencies is transparent.
Assessment	Observed.
Comment	
6.1.1	The regulatory framework and operating procedures governing the conduct of financial policies should be publicly disclosed and explained.
Description	The regulatory framework and operating procedures of the FOSI and the Cantonal Offices are specified in the law (see 5.1).
Assessment	Observed.
Comment	

6.1.2	The regulations for financial reporting by financial institutions to financial agencies should be publicly disclosed.
Description	The LLP (Article 62) gives the FOSI and Cantonal Offices the authority to request financial reporting by pension funds. The nature of this reporting is specified in the BVV2 (Articles 47-48).
Assessment	Observed.
Comment	
6.1.3	The regulations for the operation of organized financial markets (including those for issuers of traded financial instruments) should be publicly disclosed.
Description	
Assessment	Not applicable.
Comment	
6.1.4	Where financial agencies charge fees to financial institutions, the structure of such fees should be publicly disclosed.
Description	The FOSI and Cantonal Offices charges fees to the pension funds they supervise, and the structure of such fees is disclosed in regulations (VGBV).
Assessment	Observed.
Comment	
6.1.5	Where applicable, formal procedures for information sharing and consultation between financial agencies (including central banks), domestic and international, should be publicly disclosed.
Description	There are no formal procedures for information sharing among financial agencies. With regard to coordination, the law has created an advisory Federal Commission on Occupational Benefits Plans with representatives from federal and cantonal governments, employers, employees, and the pension funds.
Assessment	Observed.
Comment	The law could require more formal procedures for frequent consultation, coordination and information sharing among pension regulators and, in particular, the insurance regulator (see above, 5.2).
6.2	**Significant changes in financial policies should be publicly announced and explained in a timely manner.**
Description	Significant changes to financial policies are announced immediately after a decision has been made, through public releases to the media, publication in the official bulletin and other publications, and posting on the website.
Assessment	Observed.
Comment	
6.3	**Financial agencies should issue periodic public reports on how their overall policy objectives are being pursued.**
Description	The Public Organizations Law prescribes all federal and cantonal organizations to publish an annual report. The FOSI annual report contains a discussion of regulatory changes and financial statistics of the pension system, as well as a brief overview of supervisory actions

	and legal actions related to the pension system.
Assessment	Observed.
Comment	
6.4	**For proposed substantive technical changes to the structure of financial regulations, there should be a presumption in favor of public consultations, within an appropriate period.**
Description	The FOSI does have a presumption in favor of public consultations for proposed substantive technical changes to the structure of financial regulations.
Assessment	Observed.
Comment	The process of public consultations is extensive, with a length over three months; equally, new regulations take effect several months after the end of public consultations.
VII. PUBLIC AVAILABILITY OF INFORMATION ON FINANCIAL POLICIES	
7.1	**Financial agencies should issue a periodic public report on the major developments of the sector(s) of the financial system for which they carry designated responsibility.**
Description	The FOSI, together with the Federal Office of Statistics (BFS), publishes statistics of the pension system every two years, with a two-year delay.
Assessment	Broadly observed.
Comment	More frequent and timely disclosure of statistics of the pension system would be advisable.
7.2	**Financial agencies should seek to ensure that, consistent with confidentiality requirements, there is public reporting of aggregate data related to their jurisdictional responsibilities on a timely and regular basis**.
Description	See above, 7.1.
Assessment	Broadly observed.
Comment	Bi-annual disclosure with a two-year delay does not fully address the timeliness requirement set out in this practice.
7.3	**Where applicable, financial agencies should publicly disclose their balance sheets on a preannounced schedule and, after a predetermined interval, publicly disclose information on aggregate market transactions.**
Description	The FOSI prepares a report on its receipts and expenditures and this appears as a section in the government accounts. There is no balance sheet as all revenues are remitted to the Treasury. The FOSI does not engage in market transactions.
Assessment	Broadly observed.
Comment	
7.3.1	Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by financial agencies should be publicly disclosed through an appropriate statement when such disclosure will not be disruptive to financial stability.
Description	The Guarantee Fund's annual report contains a detailed description of emergency financial support granted to pension funds in the second pillar. A description of the objectives and roles of the Guarantee Fund is also contained in the FOSI annual report.
Assessment	Observed.

Comment	The Guarantee Fund is a foundation under public law, and is submitted to the supervision of the FOSI. The law (SFV1 Article 8) requires the Guarantee Fund to submit its accounts to the FOSI.
7.4	**Financial agencies should establish and maintain public information services.**
Description	The FOSI and the Cantonal Offices maintain public information services through their websites and various publications.
Assessment	Observed.
Comment	
7.4.1	Financial agencies should have a publications program, including a periodic public report on their principal activities, issued at least annually.
Description	Pension supervisory authorities have a publication program, including annual reports and a variety of publications posted on their websites.
Assessment	Observed.
Comment	It would be advisable that annual reports be also posted on the agencies' websites.
7.4.2	Senior financial agency officials should be ready to explain their institutions' objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.
Description	At their discretion, senior officers from the pension supervisory agencies provide interviews and participate in different public fora dealing with pension issues, in which case the text of their speeches may be released on their websites.
Assessment	Observed.
Comment	
7.5	**Texts of regulations and any other generally applicable directives and guidelines issued by financial agencies should be readily available to the public.**
Description	The texts of pension regulations are disclosed through the official bulletin, publications, and on the websites of the FOSI, the Cantonal Offices, and the Confederation. Some regulations are available to the public at a (minimal) cost.
Assessment	Observed.
Comment	
7.6	**Where there are deposit insurance guarantees, policy-holder guarantees, and any other client asset protection schemes, information on the nature and form of such protections, on the operating procedures, on how the guarantee is financed, and on the performance of the arrangement, should be publicly disclosed.**
Description	The nature and form of the Guarantee Fund is contained in the law (SFV1).
Assessment	Observed.
Comment	
7.7	**Where financial agencies oversee consumer protection arrangements (such as dispute settlement processes), information on such arrangements should be publicly disclosed.**
Description	Under the law (LPP, Articles 73-74), consumers of pension services under the second pillar can appeal to the courts under a simplified procedure, which is cost-free to consumers. The

	FOSI and the Cantonal Offices do not otherwise oversee consumer protection arrangements.
Assessment	Observed.
Comment	Discussions are underway at the FOSI to set up an office of the ombudsman with responsibility for consumer protection related to private pension funds. In addition, workers' unions provide pension-related consumer protection services to their members, and a number of nonprofit associations provide free advice on the matter. The (private) insurance ombudsman can be involved in consumer protection cases that include services provided by insurance companies.
VIII. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY FINANCIAL AGENCIES	
8.1	**Officials of financial agencies should be available to appear before a designated public authority to report on the conduct of financial policies, explain the policy objective(s) of their institution, describe their performance in pursuing their objective(s), and, as appropriate, exchange views on the state of the financial system.**
Description	Officials of pension supervisory agencies are available to appear before Cantonal Parliaments or the Federal Council.
Assessment	Observed.
Comment	Accountability before the plenary Parliament is normally by the Minister of Home Affairs (Interior) who is answerable to Parliament and is responsible for presenting legislation on the pension system.
8.2	**Where applicable, financial agencies should publicly disclose audited financial statements of their operations on a preannounced schedule.**
Description	The FOSI and Cantonal Offices are considered a part of the federal and cantonal government, respectively, for financial purposes. They are subject to audit by the government auditor.
Assessment	Not applicable.
Comment	
8.2.1	Financial statements, if any, should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.
Description	See above, 8.2.
Assessment	Not applicable.
Comment	
8.2.2	Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.
Description	The FOSI and Cantonal Offices are considered a part of the federal and cantonal government, respectively, for financial purposes, including internal audit arrangements.
Assessment	Not applicable.
Comment	
8.3	**Where applicable, information on the operating expenses and revenues of financial agencies should be publicly disclosed annually.**
Description	The FOSI and Cantonal Offices are considered a part of the federal and cantonal government, respectively, for financial purposes.

Assessment	Not applicable.
Comment	
8.4	**Standards for the conduct of personal financial affairs of officials and staff of financial agencies and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.**
Description	Rules for all civil servants apply to the staff of the FOSI and the Cantonal Offices, and are publicly disclosed.
Assessment	Observed.
Comment	
8.4.1	Information about legal protections for officials and staff of financial agencies in the conduct of their official duties should be publicly disclosed.
Description	Rules applicable to all civil servants, which are published, provide legal protection for officials and staff of the pension regulatory authorities in the conduct of their official duties. All charges are brought against the institution and not against the individual.
Assessment	Observed.
Comment	

Table 23. Summary Observance of Transparency Code—Pensions

Assessment Grade	Practices Grouped by Assessment Grade	
	Count	List
Observed	23	5.1, 5.1.2, 5.1.3, 5.1.4, 5.2, 6.1, 6.1.1, 6.1.2, 6.1.4, 6.1.5, 6.2, 6.3, 6.4, 7.3.1, 7.4, 7.4.1, 7.4.2, 7.5, 7.6, 7.7, 8.1, 8.4, 8.4.1
Broadly observed	4	5.1.1, 7.1, 7.2, 7.3
Partly observed		
Non-observed		
Not applicable	8	5.3, 5.4, 5.5, 6.1.3, 8.2, 8.2.1, 8.2.2, 8.3

Recommended action plan and authorities' response to the assessment

Table 24. Recommended Action Plan—Pension Policies Transparency

Reference Practice	Recommended Action
PENSIONS	
V. Clarity of Roles, Responsibilities, and Objectives of Financial Agencies Responsible for Financial Policies	It would be advisable that the FOSI annual report be published in a more timely fashion.
VI. Public Availability of Information on Financial Policies	More frequent and timely disclosure of statistics of the pension system would be advisable. It would also be recommendable that annual reports

Reference Practice	Recommended Action
	be posted on the agency's website.

Authorities' response

The authorities were in agreement with the assessments.

E. Transparency of Financial Policies—Payment Systems

This assessment was based on information provided by the SNB in the form of the answers to the IMF Questionnaire on Compliance with the Code of Good Practices on Transparency in Financial Policies, particularly in regard to the oversight of payment systems. This source was supplemented by discussions held with the staff of the Payment Systems Section of the SNB. The main author of this assessment is James Dingle (Bank of Canada).

Practice-by-practice assessment

Table 25. Detailed Assessment of Observance of Transparency Code—Payment Systems

V. Clarity of Roles, Responsibilities and Objectives of Financial Agencies Responsible for Financial Policies	
5.1 The broad objective(s) and institutional framework of financial agencies should be clearly defined, preferably in relevant legislation or regulation.	
Description	Article 2 of the Law on the Swiss National Bank (LNB) requires that it shall "facilitate and secure the operations of cashless payment systems."
Assessment	Observed.
Comments	
5.1.1 The broad objective(s) of financial agencies should be publicly disclosed and explained.	
Description	The inside front cover of the SNB Annual Report states the central bank's broad objectives with respect to the payment system in a more concrete fashion than in the legislation.
Assessment	Observed.
Comments	
5.1.2 The responsibilities of the financial agencies and the authority to conduct financial policies should be publicly disclosed.	
Description	The Federal Law on the Swiss National Bank (LNB) is a public document.
Assessment	Observed.
Comments	
5.1.3 Where applicable, the broad modalities of accountability for financial agencies should be publicly disclosed.	
Description	Article 2, paragraph 2 of the LNB requires that before taking economic and monetary policy decisions, the Federal Council and the SNB shall inform each other of their intentions and coordinate their efforts.
Assessment	Observed.
Comments	
5.1.4 Where applicable, the procedures for appointment, terms of office, and any general criteria for removal of the heads and members of the governing bodies of financial agencies should be publicly disclosed.	
Description	The three members of the SNB's Governing Council are elected by the Federal Council on the recommendation of the Bank Council (see Articles 53 and 63 of the LNB.) The Federal

	Government also has the power to dismiss the Board members (see Article55).
Assessment	Observed.
Comments	
5.2 The relationship between financial agencies should be publicly disclosed.	
Description	The relationship between the SNB and the Federal Government is defined in Articles 1, 2, and 63 of the LNB.
Assessment	Observed.
Comments	
5.3 The role of oversight agencies with regard to payment systems should be publicly disclosed.	
Description	The role of the SNB in payment systems is disclosed in the annual reports, in public statements, other publications and in speeches by officers.
Assessment	Observed.
Comments	A policy paper on the payment system is in preparation.
5.3.1 The agencies overseeing the payment system should promote the timely public disclosure of general policy principles (including risk management policies) that affect the robustness of systemically important payment systems.	
Description	The extensive publications on the nature of the SIC represent full disclosure of the principles and practices of the SNB with respect to risk management in this systemically important payment mechanism.
Assessment	Observed.
Comments	
5.4 Where financial agencies have oversight responsibilities for self-regulatory organizations (e.g., payment systems), the relationship between them should be publicly disclosed.	
Description	The SNB oversees the SIC, largely through its contracts with SIC AG. The SIC rules and procedures are available on request.
Assessment	Observed.
Comments	
5.5 Where self-regulatory organizations are authorized to perform part of the regulatory and supervisory process, they should be guided by the same good transparency practices specified for financial agencies.	
Description	The service corporation SIC AG, which could be viewed as a self-regulatory organization, is not concerned with the regulatory and supervisory process.
Assessment	Not applicable.
Comments	
VI. OPEN PROCESS FOR FORMULATING AND REPORTING OF FINANCIAL POLICIES	
6.1 The conduct of policies by financial agencies should be transparent, compatible with confidentiality considerations and the need to preserve the effectiveness of actions by regulatory and oversight agencies.	
Description	The conduct of policies with respect to the payment system can be viewed in a transparent environment in the SIC rules and procedures. These are available on request. In addition there is relevant material published on the SNB website, in speeches and in staff publications.

Assessment	Observed.
Comments	
6.1.1 The regulatory framework and operating procedures governing the conduct of financial policies should be publicly disclosed and explained.	
Description	As noted above, the conduct of policies with respect to the payment system can be viewed within the transparent environment of the SIC rules and procedures. These are available on request. Relevant material is published on the SNB website, in speeches and in staff publications.
Assessment	Observed.
Comments	
6.1.2 The regulations for financial reporting by financial institutions to financial agencies should be publicly disclosed.	
Description	The SIC continually creates data and reports which are frequently used in SNB publications and in presentations by central bank officials.
Assessment	Observed.
Comments	
6.1.3 The regulations for the operation of organized financial markets (including those for issuers of traded financial instruments) should be publicly disclosed.	
Description	
Assessment	Not applicable.
Comments	
6.1.4 Where financial agencies charge fees to financial institutions, the structure of such fees should be publicly disclosed.	
Description	The SNB does not charge fees for its oversight activities.
Assessment	Not applicable.
Comments	
6.1.5 Where applicable, formal procedures for information sharing and consultation between financial agencies (including central banks), domestic and international, should be publicly disclosed.	
Description	Regular meetings between the SNB and other financial agencies such as the Federal Banking Commission ensure an adequate exchange of information on payment system matters. The SNB is also a member of the BIS Committee on Payment and Settlement Systems, as listed in CPSS publications.
Assessment	Observed.
Comments	
6.2 Significant changes in financial policies should be publicly announced and explained in a timely manner.	
Description	The SNB announces and explains all significant changes in its oversight policy. This takes place through the direct notification of SIC participants, in press releases, on the central bank website, and in public speeches.

Assessment	Observed.
Comments	
6.3 Financial agencies should issue periodic public reports on how their overall policy objectives are being pursued.	
Description	The SNB publish reports on how the broad objectives (i.e., increasing the safety and soundness of the payment system) are being pursued – in its Annual Report and whenever such communications seem necessary.
Assessment	Broadly observed.
Comments	
6.4 For proposed substantive technical changes to the structure of financial regulations, there should be a presumption in favor of public consultations, within an appropriate period.	
Description	The process of preparing the revision of the LNB involved a diverse set of experts and the dissemination of their draft text of a possible new law.
Assessment	Observed.
Comments	
VII. PUBLIC AVAILABILITY OF INFORMATION ON FINANCIAL POLICIES	
7.1 Financial agencies should issue a periodic public report on the major developments of the sector(s) of the financial system for which they carry designated responsibility.	
Description	The Annual Report of the SNB regularly includes a brief report on the major developments in the payment system during the year just passed. In addition there are ad hoc public announcements on more current developments, as necessary.
Assessment	Observed.
Comments	
7.2 Financial agencies should seek to ensure that, consistent with confidentiality requirements, there is public reporting of aggregate data related to their jurisdictional responsibilities on a timely and regular basis.	
Description	The SNB publishes data on the SIC in its Monthly Statistical Bulletin. It also collects and transmits data on the payment system broadly defined and provides them to the BIS for publication in the document titled "Statistics on Payment Systems in the Group of Ten Countries."
Assessment	Observed.
Comments	
7.3 Where applicable, financial agencies should publicly disclose their balance sheets on a pre-announced schedule and, after a predetermined interval, publicly disclose information on aggregate market transactions.	
Description	The balance sheet of the SNB is published in the bank's Annual Report; a summary balance sheet is published on the 10th, 20th and last day of each month, this information becoming available on the next business day in each case.
Assessment	Observed.
Comments	

7.3.1 Consistent with confidentiality and privacy of information on individual firms, aggregate information on emergency financial support by financial agencies should be publicly disclosed through an appropriate statement when such disclosure will not be disruptive to financial stability.	
Description	The total amount of emergency lending would appear on the balance sheets appearing promptly after the 10th, 20th and last day of each month. It would be combined with "normal" Lombard advances to all banks, and all outstanding repurchase transactions. There has been no emergency support in many years, hence no examples of "appropriate statements."
Assessment	Broadly observed (see also section 3.2.3 of the assessment of monetary policy transparencies).
Comments	
7.4 Financial agencies should establish and maintain public information services.	
Description	The SNB publishes a quarterly bulletin (in French and German) and an annual report (in French, German and English). There is a public information unit in Department I that is called "Communications."
Assessment	Observed.
Comments	
7.4.1 Financial agencies should have a publications program, including a periodic public report on their principal activities issued at least annually.	
Description	Reports on specific developments, press releases, and speeches of members of the Governing Council are made public via the SNB website which is updated daily.
Assessment	Observed.
Comments	
7.4.2 Senior financial agency officials should be ready to explain their institution's objective(s) and performance to the public, and have a presumption in favor of releasing the text of their statements to the public.	
Description	Senior officials of the SNB are ready to explain the central bank's objectives as required. These explanations often involve making speeches, participating in conferences, and in some cases teaching university courses.
Assessment	Observed.
Comments	
7.5 Texts of regulations and any other generally applicable directives and guidelines issued by financial agencies should be readily available to the public.	
Description	The SNB has the legal authority under the LNB to issue ordinances; currently there are none in effect.
Assessment	Not applicable.
Comments	The future LNB is expected to lead to three ordinances: (i) detailed regulations on the oversight of the payment system; (ii) the collection of statistics; and (iii) the modalities of the reserve regime.
7.6 Where there are deposit insurance guarantees, policyholder guarantees, and any other client asset protection schemes, information on the nature and form of such protections, on the operating procedures, on how the guarantee is financed, and on the performance of the arrangement, should be publicly disclosed.	
Description	

Assessment	Not applicable.
Comments	
7.7 Where financial agencies oversee consumer protection arrangements (such as dispute settlement processes), information on such arrangements should be publicly disclosed.	
Description	The SNB does not oversee consumer protection arrangements.
Assessment	Not applicable.
Comments	
VIII. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY FINANCIAL AGENCIES	
8.1 Officials of financial agencies should be available to appear before a designated public authority to report on the conduct of financial policies, explain the policy objective(s) of their institution, describe their performance in pursuing their objective(s), and, as appropriate, exchange views on the state of the financial system.	
Description	Senior SNB officials appear regularly before the Federal Government (the focus naturally being the conduct of monetary policy). Views on the development of the economy and the financial system are exchanged periodically with the Federal Department of Finance, the State Secretariat for Economic Affairs, and the Federal Banking Commission.
Assessment	Observed.
Comments	
8.2 Where applicable, financial agencies should publicly disclose audited financial statements of their operations on a pre-announced schedule.	
Description	The SNB is an independent public-law institution in the form of a joint-stock company. It is thus required to have external auditors who report to the annual meeting of shareholders, which is public.
Assessment	Observed.
Comments	
8.2.1 Financial statements, if any, should be audited by an independent auditor. Information on accounting policies and any qualification to the statements should be an integral part of the publicly disclosed financial statements.	
Description	The SNB, as a joint-stock company, must apply the Swiss Accounting and Reporting Recommendations. As noted above, an external firm audits the financial statements.
Assessment	Observed.
Comments	
8.2.2 Internal governance procedures necessary to ensure the integrity of operations, including internal audit arrangements, should be publicly disclosed.	
Description	
Assessment	Not observed (see also section 4.2.2 of the monetary policy transparency assessment).
Comments	
8.3 Where applicable, information on the operating expenses and revenues of financial agencies should be publicly disclosed annually.	

Description	Expenses and revenues are disclosed in detail in a financial report published by the SNB each April.
Assessment	Observed.
Comments	
8.4 Standards for the conduct of personal financial affairs of officials and staff of financial agencies and rules to prevent exploitation of conflicts of interest, including any general fiduciary obligation, should be publicly disclosed.	
Description	
Assessment	Not observed (see section 4.4 of the monetary policy transparency assessment).
Comments	
8.4.1 Information about legal protections for officials and staff of financial agencies in the conduct of their official duties should be publicly disclosed.	
Description	Article 59 of the LNB states that officials and employees of the SNB are subject to federal legislation concerning the responsibility of federal officials under civil penal law. The Federal Law on the Liability of the Confederation, its authorities and officials applies. The Confederation has the right of recourse against an officer of the SNB only if such person acted with intent or gross negligence. Criminal prosecution of Federal officers is permitted only with the agreement of the Federal Department of Justice and Police.
Assessment	Observed.
Comments	

Table 26. Summary Observance of Transparency Code—Payment Systems

Assessment grade	Practices grouped by assessment grade	
	Count	List
Observed	26	5.1, 5.1.1, 5.1.2, 5.1.3, 5.1.4, 5.2, 5.3, 5.3.1, 5.4, 6.1, 6.1.1, 6.1.2, 6.1.5, 6.2, 6.4, 7.1, 7.2, 7.3, 7.4, 7.4.1, 7.4.2, 8.1, 8.2, 8.2.1, 8.3, 8.4.1
Broadly observed	1	6.3, 7.3.1
Partly observed		
Non-observed	2	8.2.2, 8.4
Not applicable	6	5.5, 6.1.3, 6.1.4, 7.5, 7.6, 7.7

Recommended action plan and authorities' response to the assessment

No further action needs to be undertaken in the area of payment system policy transparency. For responses on general transparency issues, see monetary policy transparency assessment. The authorities were in agreement with this assessment.