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TECHNICAL NOTE ON SECURITIES MARKET—SELECTED ISSUES IN REGULATION AND SUPERVISION

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TECHNICAL NOTE

SECURITIES MARKET: SELECTED ISSUES IN REGULATION AND SUPERVISION

Prepared By

Monetary and Capital Markets Department

This Technical Note was prepared by Nila Khanolkar in the context of the Financial Sector Assessment Program in Switzerland, led by Oana Croitoru. It contains technical analysis and detailed information underpinning the FSAP's findings and recommendations. Further information on the FSAP can be found at http://www.imf.org/external/np/fsap/fssa.aspx

CONTENTS

Glossary

AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
AMLA	Anti-Money Laundering Act of 10 October 1997
AUM	Assets Under Management
CIS	Collective Investment Scheme
FDF	Federal Department of Finance
FinIA	Financial Institutions Act of 15 June 2018
FINMA	Swiss Financial Market Supervisory Authority
FINMASA	Financial Market Supervision Act of 22 June 2007
FinMIA	Financial Market Infrastructure Act of 19 June 2015
FinSA	Financial Services Act of 15 June 2018
FSAP	Financial Sector Assessment Program
FSB	Financial Stability Board
GDP	Gross Domestic Product
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
MMF	Money Market Fund
SIF	Staatssekretariat für Internationale Finanzfragen (The State Secretariat for International Financial Matters)
SO	Supervisory Organization
SRO	Self-Regulatory Organization
TN	Technical Note

EXECUTIVE SUMMARY

Switzerland has a large securities market and one of the world's largest asset and wealth management industries, where banks play a dominant role. Swiss asset managers manage CHF 7.87 trillion in assets, among others CHF 1.3 trillion in collective assets and CHF 1.9 trillion in discretionary mandates.[1] Banks, directly and at a group level, manage most of these assets and generate a substantial part of their revenues from asset and wealth management activities. The secondary market in Switzerland leads the market share of trading in Swiss equities globally, including in three of the top ten shares in Europe by market capitalization. Securities trading is concentrated in one trading venue, under the SIX group, which manages practically the entire financial markets infrastructure in the country. Banks are dominant shareholders of the trading venue/ group and the leading broker-dealers.

Major progress has been made to the legal, regulatory, and supervisory framework since the last FSAP. The legal framework for asset management industry underwent an overhaul with two new Acts coming into force in 2020. The new framework, among others, introduced a new licensing regime for portfolio managers and trustees, who did not previously require licensing. In addition, substantial improvements were made to the collective investment scheme (CIS) framework, particularly with respect to liquidity risk management, reporting, and supervisory process, implementing several recommendations from the previous FSAP. A new licensing framework for distributed ledger technology (DLT) based trading facilities was introduced in 2021. Several key reforms to the framework for trading systems are underway, particularly relating to market abuse, which if implemented, will strengthen the current framework.

There is significant scope for further improvements to the legal, regulatory, and supervisory framework for securities markets. These include improvements in organizational structure and resources within FINMA; plugging data gaps; enhancing the regulatory framework; filling of gaps in the supervisory perimeter; improvements to FINMA's supervisory regime; and expanding FINMA's investigation and enforcement powers (elaborated subsequently).

FINMA should adopt substantial improvements to its organizational structure and supervisory framework. FINMA's organization structure should reflect the cross-sectoral nature of asset management and trading activities, permitting a holistic view and a consistent approach. Data gaps, which are substantial, should be plugged on priority and related reporting frameworks should be strengthened. While there has been some enhancement of resources since the last FSAP for securities market, the sheer size and scale of the industry requires further strengthening, particularly for asset and wealth management activities of banks and for trading systems. FINMA should improve its own supervisory efforts and limit reliance on regulatory auditors to compliance-based audits. At the same time, it should continue its efforts to strengthen its supervisory framework: enhance reporting requirements; disclose publicly supervisory expectations to supplement principle-based regulations; improve focus on certain key risks in the risk-based supervision process; and adopt an outcome-based periodic review of the entire process. FINMA should improve its market

[1] As per data provided by the authorities. However, as discussed through the technical note, data gaps are significant and affect calculation of this figure.

monitoring, particularly on trading outside venues and shifts in liquidity patterns, enabling it to periodically identify shifts in potential risks and adjust its supervisory process accordingly.

The regulatory framework should continue to be upgraded in line with international standards; gaps in the supervisory perimeter should be plugged and legal impediments to effective supervision and enforcement removed through changes to the legal framework. Regulatory work on implementing FSB and IOSCO standards on liquidity risk management for open-ended funds should be a priority. Gaps in FINMA's supervisory perimeter should be plugged: pure investment advisory and distribution services should be subject to supervision (preferably under a holistic licensing, regulatory and supervisory regime); the legal basis for SRO- FINMA cooperation should be laid down and FINMA's powers over SROs should be strengthened in line with IOSCO principles. Legal impediments that may constrain FINMA from expressing its supervisory expectations should be removed. Effectiveness of the current supervisory framework for portfolio managers and trustees and the overall licensing, regulatory and supervisory framework for prospectus review functions should be analyzed and reviewed and based on the outcome, reforms to the legislative framework should be undertaken, if necessary. The ongoing reforms for financial market infrastructures, including trading systems, should be implemented as a priority, particularly relating to market abuse. FINMA must be empowered with adequate investigative and enforcement tools, particularly powers to fine individuals, to enable effective enforcement of market abuse cases.

Table 1. Switzerland: Main Recommendations

#	Recommendations	Addressee	Timing[1]	Priority[2]
1.	FINMA should undertake a cross-sectoral reorganization of its oversight of asset management activities and increase resourcing of supervision of asset and wealth management activities, particularly by banks. (¶47, 51)	FINMA	MT	H
2.	Data gaps should be plugged on priority and related reporting requirements should be enhanced. (¶14, 46, 60, 91)	FINMA	ST	H
3.	FINMA should improve its supervisory framework for asset management and trading systems through targeted improvements. (¶25, 48, 49, 50, 98, 99)	FINMA	MT	H
4.	The regulatory framework for asset management should be further strengthened through priority implementation of FSB and IOSCO recommendations on liquidity risk management. (¶38)	FDF	ST[3]/MT	M
5.	Gaps in the supervisory perimeter should be filled by providing necessary powers to FINMA; any legal impediments for FINMA to disclose its supervisory expectations should be removed. (¶24, 49, 77, 100)	FDF	MT	M

Table 1. Switzerland: Main Recommendations (Concluded)				
#	Recommendations	Addressee	Timing[1]	Priority[2]
6.	FINMA should improve market monitoring, particularly relating to off-venue trading, organized trading facilities (OTFs), aspects affecting market liquidity, and short-selling. (¶60, 61, 90, 91)	FINMA	ST	H
7.	Mechanisms to prevent, detect, and enforce market abuse should be enhanced, including through implementation of proposed reforms, improvement in requirements for issuers and supervised entities, better ability to detect market manipulation, and enhancing FINMA's investigative and enforcement powers. (¶78, 79, 80, 81)	FDF, FINMA	MT	H

[1] ST = Short Term (Within 2 years); MT = Medium Term (3-5 years); LT: Long Term (more than 5 years)

[2] H = High; M = Medium; L = Low.

[3] Work on FSB and IOSCO recommendations should start in the short term; implementation can be extended to medium term.

INTRODUCTION

A. Scope and Approach

1. This technical note (TN) focuses on two key areas in Switzerland's securities market: asset management and trading systems. Since the asset management oversight framework was reviewed in a TN in detail in the 2019 FSAP, this note focuses on the updates to the regulatory and supervisory framework since then.[2] Despite being an update, the emphasis on the asset management section is substantial since the size of the industry is significant and major revisions to the regulatory and supervisory framework have taken place in the last five years. For trading systems and related aspects, the last review was done in 2014 in a detailed assessment of all the IOSCO principles, while some aspects were touched upon in two TNs relating to fintech and financial market infrastructures in the previous FSAP in 2019.[3] Accordingly, this note delves deeper into the regulatory and supervisory framework of the trading systems, while focusing also on the updates since the previous assessments. In both cases, particular emphasis has been placed on regulatory and supervisory issues with most direct relevance for financial stability. While not being an assessment against IOSCO principles, it draws on relevant IOSCO Objectives and Principles of Securities Regulation and other FSB and IOSCO recommendations related to the topics.[4]

[2] Switzerland: Financial Sector Assessment Program; Technical Note-Regulation and Supervision of Asset Management Activities (imf.org), June 2019.

[3] Switzerland: Detailed Assessment of Implementation—IOSCO Objectives and Principles of Securities Regulation; IMF Country Report 14/266; September 2014; Switzerland: Financial Sector Assessment Program; Technical Note-Supervision and Oversight of Financial Market Infrastructures.

[4] IOSCO Principles 24-28 (Collective Investment Schemes), Principles 33-37 (Secondary and other markets), and other principles, relevant directly or indirectly to asset management and trading systems. The review also draws from detailed IOSCO and FSB recommendations/guidance on various sub-topics relating to the above two areas, in particular those that have been issued since the last FSAP (FSB and IOSCO recommendations relating to open-ended funds in 2023).

2. This review is based on various written documentation as well as on-site meetings with the authorities and other stakeholders. The author heavily relied on the response to the questionnaire and data provided by the authorities for an overview of the broad industry, the regulatory and supervisory framework, and its implementation in practice. Public materials including the relevant Acts, Ordinances, circulars, guidance, self-regulation, and other materials on authorities' websites were reviewed either in detail or at a broad level, depending on the need. On-site/ virtual meetings with the authorities (FINMA and the State Secretariat for International Financial Matters (SIF)) and representatives of the industry, investors, auditors, and SROs, provided additional key information and clarity on various topics.[5] On-site meetings also included supervisory review of certain files, focusing primarily on certain licensing, supervisory, and enforcement case files.[6]

3. The author is grateful to the authorities and representatives of the industry, auditors, SROs, and investors, for their cooperation. The author benefitted greatly from the valuable inputs and insightful views from meetings with all the participants. The author is particularly grateful to Ms. Julia Simola and Ms. Aline Waeber from FINMA and Mr. Alain Geier from State Secretariat for International Finance (SIF) for their immense work in coordinating the activities of the workstream. The author also expresses her gratitude to asset management and markets divisions of FINMA and the capital markets team of SIF, whose insights were not only useful but fundamental to the drafting of this TN.[7]

B. Institutional and Legal Framework[8]

4. FINMA is the supervisor for securities market, which fits within the larger role of the institution as an integrated cross-sectoral supervisor. FINMA was established in 2009 as the institution resulting from the merger of then existing sectoral supervisors for banking, insurance, and anti-money laundering. FINMA's powers over the securities market (as well as other sectors) are primarily derived from the Federal Act on the Swiss Financial Market Supervisory Authority, 2007 ("FINMASA") and the other relevant sectoral and cross-sectoral Acts.

5. The regulatory framework for securities market is principle-based with the bulk laid down under legislation and federal ordinances; FINMA Ordinances, circulars and self-regulation apply at technical levels. Details of the relevant legislative and regulatory framework are covered under the two sections of the TN respectively. FINMA is involved in the regulatory process at the level of legislation and federal ordinances and can express its opinions; but the key institution that leads this process is the SIF, a division of the Federal Department of Finance. FINMA

[5] The author was on-site in Switzerland, as a part of the first mission, between Oct 28-Nov 12, 2024.

[6] Since the relevant files and documentation were in German, the author (not well-versed with the language) primarily relied upon the authorities' live translation and guidance on the said documents.

[7] Asset management division: Noélie Läser, Valeska Stoll, Daniel Bruggisser, Renate Schmits, Laura Tscherrig, Samuel Frösch, Christian Kunz, Dorothée Ignatz, Christian Perren, Markus Schmid, Céline Buvelot, Xavier Schuwey. Markets division: Andreas Bail, Dorothee Kammerer, Thomas Güntensperger, Stefan Pankoke, Cornelia Rösler, Enforcement division: Patrik Goebel, Rico von Allmen. SIF: Julie Tomka, Sarah Jungo, Eszter Major.

[8] This Technical Note only discusses the institutional and legal framework, as it pertains to securities market. Issues related to FINMA's institutional structure, as an integrated regulator, are dealt with at great length in the detailed assessment principles for Basel Core Principles for banks, and hence, not repeated here.

regulates at a technical level through FINMA ordinances, and circulars; circulars being enforceable only in conjunction with the key legislative and ordinance provisions. FINMA's regulatory powers are restricted insofar as it can only issue regulation where it is expressly authorized to do so under the legislation. Self-regulation (recognized by FINMA and otherwise) is a very important element in Switzerland's regulatory framework as outlined later in various parts of the TN. Principles-based regulation is a key feature of Switzerland's regulatory framework for all sectors, including securities markets.

6. A uniquely dual supervisory approach is followed in Switzerland, whereby in addition to FINMA's own supervisory roles, substantial supervision is done by auditors, supervisory organizations, and self-regulatory organizations (SROs).[9] FINMA relies strongly on supervision by auditors across its functions, including in securities markets. The auditors, referred to as 'regulatory auditors', are licensed audit firms that are under the supervision of the Federal Audit Oversight Authority (FAOA) and are appointed and paid by the supervised institutions. FINMA has issued a new ordinance in 2024 and a circular on its practice concerning audit. For institutions of material importance, FINMA is involved intensely in the scoping of the audit.[10] In addition to auditors, in certain areas, the legislation accords supervisory powers to SROs and supervisory organizations, who often further use auditors in the exercise of their own supervisory functions.[11] This complex supervisory framework is explored in detail under the two sections in this note. In addition, FINMA may appoint institutions called 'audit agents' and 'investigating agents' on a case-by-case basis which are mainly entities such as auditors and lawyers appointed by FINMA (unlike regulatory auditors appointed by the entities) to exercise certain supervisory, investigative, and enforcement functions.

7. Licensing of financial institutions is primarily done by FINMA. For securities market, this includes licensing of a wide variety of entities including funds, fund management companies, managers of collective assets, portfolio managers, trustees, custodians, financial market infrastructures, among others. Some role is also accorded to Swiss National Bank (SNB), SROs, and other institutions in the licensing process in some very specific areas. For instance, licensing of systemically important financial market infrastructure requires involvement of the SNB**.** While strictly not a licensing activity, prospectus review is a significant function done by prospectus offices, currently housed under the exchange SROs. SROs/ supervisory organizations also act as 'registers of client advisors' whereby individual client advisors of unlicensed and unsupervised institutions are 'registered' which permits such persons to offer financial services such as pure investment advice and distribution.

[9] This Technical Note focuses on the role of auditors specific to the topics covered in this Note; for the detailed recommendations relating to this topic, please refer to the detailed assessment report on banking regulation and supervision.

[10] Institutions of material importance in this context refers to supervised institutions in FINMA Supervisory Categories 1 and 2 as explained later.

[11] Supervisory organization (SO) is a unique institution in the Swiss supervisory framework to whom supervision of portfolio managers and trustees is assigned under the legislation; SO falls under FINMA supervision. The auditors referred to in above sentence are licensed auditors, but not under oversight of the FAOA.

8. Administrative enforcement is primarily done by FINMA; some powers lie with SROs, and criminal offenses involve FINMA coordination with the Office of Attorney General. FINMA employs various enforcement tools including reprimand, banning individuals from practicing profession, revoking licenses, disgorgement, etc.[12] SROs also have certain enforcement powers. For instance, SROs of trading venues have substantial enforcement powers with respect to enforcing their own rules and regulations. Criminal offences, for instance relating to market abuse, involve FINMA's close cooperation with the Office of Attorney General.

9. FINMA adopts a mix of sectoral and cross-sectoral approaches in its organizational structure. It has 8 divisions: 4 sectoral (banks, insurance, markets, and asset management) and 4 cross-sectoral (enforcement, supervisory policy & legal expertise, recovery and resolution, and operations). Securities markets- related regulatory and supervisory responsibilities are conducted primarily by the asset management and markets division, while other divisions handle certain securities markets related functions (e.g., conduct supervision team). The teams closely collaborate with each other, as required.

ASSET MANAGEMENT[13]

A. Overview of the Asset Management Industry

10. Supervised entities in Switzerland can undertake asset management under different licenses.[14] As outlined later, the Financial Institutions Act (2020) brought in a licensing cascade whereby a higher category license permits other services under the same license. This has created a complicated licensing set-up whereby asset management (of CIS and individual/separate mandates) can be done under several licenses. A bank can manage collective assets as well as individual mandates under its banking license.[15] In practice, many banks have created separate entities and obtained separate licenses for their CIS related activities, while managing individual client assets under the banking license. A 'fund management company' primarily does the function of fund administration and issuance of CIS units in practice but can also manage CIS and individual client assets under the same license. In practice, fund management companies often delegate CIS asset management to 'managers of collective assets'. Such managers of collective assets can also manage individual client assets under the same license. The license of a portfolio manager is the lowest in the licensing hierarchy which permits the entity to mainly manage individual client assets; however, the license also permits management of CIS for qualified investors under certain thresholds. An

[12] Recommendations relating to strengthening of FINMA's enforcement powers in general are covered in detail under the detailed assessment of principles for banking regulation and supervision. This Note will focus on the enforcement framework relating to asset management and trading systems.

[13] This section covers management of collective investment schemes as well as individual client mandates, including wealth management by banks under the banking license. While data covers asset management by insurance, where available, the oversight is covered in greater detail in the technical note on insurance regulation and supervision.

[14] Relevant legislation for asset managers includes mainly CIS Act (CISA), Financial Institutions Act (FinIA) and Financial Services Act (FinSA). Discussion about these Acts follow in the section pertaining to FinIA and FinSA.

[15] Within a banking group, however, the holder of the dedicated license for acting as a fund management company must be a company separate from the bank.

insurance company can also undertake asset management services, but within the remit of the Insurance Act.

Table 2. Switzerland: Licensing Cascade Under FinIA		
Sr. No	**License**	**Activity permitted under FinIA under the same license**
1.	Bank	Securities firm, manager of collective assets, portfolio manager, and trustee
2.	Securities Firm	Manager of collective assets, portfolio manager, and trustee
3.	Fund management company	Manager of collective assets, portfolio manager
4.	Manager of collective assets	Portfolio Manager

11. Asset managers based in Switzerland manage approximately CHF 7.87 trillion of assets, based on data received from FINMA (see table 3 below). This includes, among others, management of collective investment schemes (CIS) (~CHF 1.3 trillion) and discretionary client mandates of ~CHF 1.9 trillion. Banks, directly or at a group level, manage a substantial portion of these assets, primarily as individual mandates (often included under the bank's wealth management business).[16] Portfolio managers, recently brought under the licensing regime, manage ~CHF 250 billion. While the figures in the table below show the aggregated AUM figures, granular details of execution only and advisory services are not available for all sectors. The figures in the table below also suffer from other data gaps, as elaborated in the notes provided below the table.

Table 3. Switzerland: Assets Managed by Asset Managers Based in Switzerland (CHF bn)[1]				
Sr. No.	**Type of asset management service**	**By fund management companies and managers of collective assets**	**By banks under the banking license[2]**	**By portfolio managers[5]**
1	**CIS**	**1,264.21**	**324.19**	**4.97**
	- Domestic CIS	544.43	307.96	0.24
	- Foreign CIS	719.78	16.23[3]	4.73
2	**Discretionary mandates**	**649.88**	**1,000.48**	**244**
3	**Total AUM** ***(incl. execution-only and advisory services, except for portfolio managers)***	**2,770.67**	**4,859.39[4]**	**248.97**
TOTAL ASSETS UNDER MANAGEMENT		**7879,03[6]**		

[1] The table includes only figures on assets managed under the licenses mentioned thereunder. The table is compiled based on the domicile of the asset manager.

[2] If a bank has a separate fund management company / manager of collective assets license, it is included in the first column.

[3] This only includes foreign CIS with AuM > CHF 500 mn. and alternative investment strategy.

[4] Based on data "Assets under Management" delivered by banks according to FINMA Accounting Ordinance, FINMA-Circular 01/20 (Appendix 4, cm 216-229) and FINMA Circular 08/14. It covers only AuM from Swiss single banks, not from other entities of Swiss banking group.

[5] The assets under management are calculated based on the information provided in the licence application forms.

[6] Can include double counting.

[16] This figure is likely to be higher since data for foreign CIS managed by banks below CHF 500 million (with non-alternative strategy) is not available.

12. Switzerland-domiciled CIS have an AUM of CHF 1.3 trillion; data gaps hinder understanding of size of foreign CIS marketed to Swiss investors. Swiss domiciled CIS are managed mainly by managers based in Switzerland, primarily under the licenses of fund management company and managers of collective assets. Foreign managers manage only ~CHF 150 billion (11%) of Swiss CIS assets. Approximately one-third of the Swiss CIS AUM are single investor funds. These funds have only one investor, have separate provisions under the CIS Act and are created primarily for institutional investors such as pension funds (72%) and insurance companies (17%).[17] 99.6% of the Swiss domiciled CIS (by Net Fund Assets) are open-ended funds.[18] ~80% are equity funds, fixed income funds and mixed funds. Alternative Funds are very small, 0.67% of total net fund assets (NFA). Money Market Funds (MMFs) and real estate funds are 3.5% and 5.7% respectively, by NFA. More than 8500 approved foreign CIS are marketed to Swiss retail investors, but data gaps hinder understanding of the size of these foreign CIS. Data on foreign CIS marketed to non-retail investors and on banks managing foreign CIS (non-alternative strategy) below CHF 500 mn are not available.

Recommendation

13. FINMA should prioritize plugging data gaps in the asset management sector. Current data gaps are substantial and comprehensive monitoring of the asset management industry is absent given cross-divisional fragmentation.[19] This prevents FINMA from obtaining a holistic view of the asset management industry, which is large and highly interconnected, particularly with the banking sector. FINMA should start with compiling a clear set of data that is already available within FINMA across various divisions. Such compilation should enable clear identification of data gaps that prevent FINMA from obtaining a clear and holistic picture of different types of asset management activities and entities carrying out such activities under various licenses. This should then result in a review of the current reporting framework to plug the necessary data gaps. Specific data gaps with respect to the CIS sector is covered in a separate recommendation under the supervision section.

B. Scope and Approach

14. This Section focuses on key developments in the asset management industry since the last FSAP. These include (i) Introduction of a new legislative framework (FinIA and FinSA) governing licensing, regulation, and supervision of the asset management industry (ii) Introduction of a new type of CIS- Limited Qualified Investor Fund (L-QIF) (iii) Substantial revisions to the regulatory and

[17] Single investor funds need a fund management company and a custodial bank, but the investor can, if certain criteria are fulfilled, manage assets on its own without an external manager. Governance, operational efficiency, tax, and transparency are cited as common benefits of a single investor fund.

[18] In practice, most open-ended funds are structured as contractual funds, although the legal framework also permits investment companies with variable capital (SICAVs). Similarly, closed-ended funds are usually structured as Limited Partnerships for Collective Investments (LPCIs), although investment companies for fixed capital (SICAFs) are also permitted.

[19] A subsequent recommendation deals with FINMA reorganization with respect to asset management in more detail.

supervisory framework relating to CIS liquidity risk framework, and (iv) Supervision and enforcement.

C. Introduction of the New Legislative Framework: Financial Institutions Act (FinIA) and Financial Services Act (FinSA)

15. The introduction of FinSA and FinIA in 2020 had significant impact on the asset management industry. Prior to introduction of these two Acts, the Collective Investment Services Act (CISA) governed licensing, regulation, and supervision of both funds as well as fund managers. With the introduction of FinIA and FinSA, CISA evolved into purely fund-specific legislation, while the framework for licensing and regulation of fund managers was transferred to FinIA and conduct requirements for fund managers included under FinSA. While FinIA and FinSA are broader in scope than asset management, this TN focuses on the framework applicable to asset management.

16. FinIA introduced a licensing cascade permitting several activities under the same license. As mentioned earlier, this resulted in asset management activity being permitted under several licenses. The cascade includes the following five categories in decreasing order of regulatory intensity: (i) securities firms (ii) fund management companies (iii) managers of collective assets (iv) portfolio managers and (v) trustees (See Table 2 above for more details). A bank can operate as a securities firm, a manager of collective assets, a portfolio manager, and a trustee without a separate license. Similarly, a securities firm can operate as a manager of collective assets, a portfolio manager, and a trustee; a fund management company as a manager of collective assets and a portfolio manager; a manager of collective assets as a portfolio manager. While multiple license requirements have been dispensed with, this does not mean an automatic permission to carry out a new activity; every new service not authorized earlier needs prior approval of FINMA.

17. FinIA introduced new licensing requirements for portfolio managers and trustees, and also brought managers of occupation pension schemes into scope. Portfolio managers and trustees were not required to be licensed before FinIA and were only subject to AML/CFT requirements.[20] Introduction of a new licensing, regulatory and supervisory framework for these entities was a substantial enhancement to the regulatory and supervisory framework for the asset management industry. Importantly, this had been recommended by the IMF in multiple FSAPs since 2002[21] and recognized by FINMA itself in its post-global financial crisis position paper in 2012.[22] In addition, management of occupational pension schemes now requires a license as a manager of collective assets or, below a certain threshold, as a portfolio manager. Managers of sub-threshold CIS now need a portfolio management license.

[20] It is important to note that most of these asset managers are smaller in size. Large portolio managers generally do so under the higher licensing categories under FinIA such as banks, securities firms, fund management companies and managers of collective assets.

[21] Switzerland: Financial System Stability Assessment, including Reports on the Observance of Standards and Codes on the following topics: Banking Supervision, Securities Regulation, Insurance Regulation, ayment Systems - ISCR/02/108

[22] Regulation of the production and distribution of financial products (FINMA position paper on distribution rules)

18. While FINMA licenses portfolio managers and trustees, the supervision is delegated to supervisory organizations (SOs). FINMA is responsible for licensing and supervising SOs. Five SOs have been licensed by FINMA and have commenced their activities. FINMA remains responsible for approving any change to the facts on which the portfolio manager license is based, as well as for enforcement. As part of the licensing process, applicants must select one of the authorized SOs, which do a preliminary vetting of the application before sending it to FINMA. SOs are financed through the fees on the supervised institutions. SOs mainly use regulatory auditors for their supervisory functions.

19. Since the last FSAP, FINMA undertook a massive administrative exercise in licensing portfolio managers and trustees, as well as new managers of collective assets. By the end of the transitional period (Dec 2022), FINMA had received a total of 1699 license applications (1,534 from portfolio managers and 165 from trustees, including both existing and newly established institutions). Based on data available end-October 2024, 90% of the applications submitted at the end of the transitional period had been processed; fewer than 160 applications were pending. FINMA hired several staff on contract to deal with the licensing process and proposes to retain several for supervisory and other functions. In addition to portfolio managers and trustees, several license applications were received for acting as managers of collective assets as management of occupational pension schemes were brought into scope, which also resulting in increase in licensing applications over the last 5 years.

20. Complementing FinIA, another piece of legislation- FinSA - was introduced as a cross-sectoral law governing conduct of financial service providers and prospectus requirements. FinSA has its roots in the global financial crisis, post which FINMA issued a position paper in 2012 which led to a holistic legislative reform, resulting finally in the introduction of the two new laws in 2020. FinSA is largely modelled on EU Markets in Financial Instruments Directive (MiFID) II. It standardized conduct requirements relating to transparency, conflicts of interest, due diligence obligations, among others. Being cross-sectoral, FinSA applies to all financial service providers including asset managers. FinSA also has a section on prospectus requirements applicable to issuers.

21. FinSA applies differentiated conduct requirements depending on the type of client and type of service provided. Financial providers are required to segment their clients into private customers, professional, and institutional clients, and the law accords decreasing level of protection in that order. The framework provides for 'opt in/ out' regime enabling clients to move from one segment to another.[23] Further, retail clients who have entered into an investment management or an advisory agreement on a long-term basis with a regulated financial institution are deemed to be qualified investors under the revised CISA. Provision of portfolio management service requires suitability assessment. For investment advisory activity, portfolio-related advice requires suitability assessment while transaction-related advice requires only appropriateness assessment (a less comprehensive assessment than suitability assessment). No suitability or appropriateness tests are required for institutional clients and have limited applicability for professional clients. While broadly

[23] The regime permits clients to seek higher or lower level of investor protection. E.g., a professional client can choose to be classified as a retail client. A High Net Worth Individual (HNI) fulfilling asset/ experience/ expertise criteria can ask to be treated as a professional client, subject to certain conditions.

based on EU MiFID II, requirements under FinSA are relaxed in certain aspects, for instance with respect to client classification, suitability requirements, and execution-only services for complex products to retail clients.

22. Distribution and investment advisory services are now governed under a 'client adviser' regime under FinSA.[24] Client advisers are natural persons who perform financial services on behalf of a financial service provider or in their own capacity as financial service providers. If the client adviser is employed by a supervised financial institution, no registration is required. Client advisors acting in their own capacity or employed by unsupervised institutions are required to be registered in a 'register of advisers'. In practice, this primarily affects entities and persons providing pure distribution or pure investment advisory services, since currently no separate license is required for these activities. It must be noted that distributors were earlier required to be licensed under the CISA, which was done away with post FinSA.[25]

Recommendations

23. Pure investment advisory and distribution services should be subject to supervision. Currently, pure investment advisers and distributors who do not offer other licensed financial services are currently governed under the 'client adviser' framework. As mentioned above, this framework requires registration of the individuals who offer such advice or distribution with a client register and regulations under FinSA apply (e.g., transparency). However, there is no corresponding supervision. The framework relies on an Ombudsman regime and civil courts for addressing disputes relating to such services, which cannot be a substitute for supervision. The effectiveness of a regulatory framework with a corresponding supervisory framework is questionable. Even if pure investment advisory services may be considered lower on the risk spectrum compared to other services, at the very minimum, a basic reporting and supervisory framework, with supervisory powers assigned to FINMA should be in place. It will then be within FINMA's discretion to determine the intensity and frequency of supervision of such entities, based on the risk level (derived from supervisory data). The Swiss regulatory framework has come a long way by scoping in portfolio managers and trustees into the licensing, regulatory and supervisory regime. A logical next step would be to plug the remaining gaps in the supervisory perimeter and bring pure investment advisors and distribution into the supervisory regime. This will bring Switzerland at par with corresponding international regimes. The authorities should preferably consider upgrading to a more holistic licensing, regulatory and supervisory framework for such activities.

24. The current supervisory structure for portfolio managers and trustees through supervisory organizations should be reviewed for quality of supervision, effectiveness, and efficiency. The current structure of supervision with multiple supervisory organizations (SOs) is unique to portfolio managers and trustees and has several areas of concern. Firstly, competition

[24] The term 'distribution' here and in the rest of the TN is to be understood in the context of the general usage of the term. With the legal context in Switzerland, such activity falls under the framework for investment advice.

[25] Explanation to FinSA states that distributors being licensed but not supervised under the earlier regime created misunderstanding among customers that these were supervised and therefore, this was replaced with a registration regime.

among SOs coupled with discretion for the entity to choose its own SO could lead to 'SO shopping' and a race to the bottom, with a potential lowering of standards, in areas where the SO has discretion. With such discretion, multiplicity could also lead to natural differences in the supervisory practices, intensity, processes, and reporting. Secondly, SOs themselves mainly rely on auditors for supervision, and therefore, adding another layer appears redundant. Several of the supervisory functions already involve FINMA in practice which practically has already resulted in duplication of work and efforts. Thirdly and importantly, there are conflicts of interest in the SOs undertaking supervision through governance and other structures.[26] Finally, at a broad level, the overall structure of having another supervisory institution for securities market (in addition to auditors and SROs) further fragments the overall supervisory institutional structure. Given these concerns, this structure should be subject to a review for its supervisory quality, effectiveness, and efficiency, given potential conflicts of interest and other concerns raised above. Such a review could be included as a part of FINMA's ongoing supervision of the SOs, the findings from which can be included in FINMA's report to FDF. This could be followed up with reforms, as may be necessary, such as strengthening of the regulatory requirements around conflicts of interest (including profit-related incentives), efforts to remove duplication of supervisory efforts and in case of fundamental structural issues or inefficiencies, direct supervision of such entities by FINMA (in line with the existing supervisory structure for other supervised entities in the securities market). Such a review will also provide necessary inputs to legislative reforms needed, if any, in the next FinIA/FinSA review.

25. FINMA should consider publishing information on the exemptions granted from licensing for asset management activities (e.g., in a summary format). Currently, FINMA processes several exemption applications which essentially are letters from FINMA confirming that the said entity is exempt from licensing. It is understood that such letters are often sought by service providers such as banks. While fees are charged for this purpose by FINMA, given that FINMA is already resource constrained, this is a waste of valuable supervisory time and resources, especially for standardized applications. Publishing information on exemptions, even if in a summary format, will provide clarity to the industry that may obviate obvious and standard exemption applications and reduce corresponding allocation of supervisory resources. In addition, this will improve overall transparency of FINMA's processes.

D. Limited Qualified Investor Fund

26. A new category of alternative fund called limited qualified investor fund (L-QIF) was introduced in 2021, effective from March 1, 2024. L-QIF can only be offered to qualified investors. If the fund is open-ended, it must be managed by a Swiss fund management company and if closed-ended, by a Swiss manager of collective assets.[27] The fundamental feature of the product is that it does not require a license or approval from FINMA and is meant to help industry from a time-to-market perspective. The fund is modelled on the lines of similar funds in Europe (e.g., RAIFs in Luxembourg) and introduced with a competitiveness objective. 8 L-QIFs have been

[26] For instance, persons charged with the administration of SOs could be representatives of the industry. There is no explicit prohibition on the SOs to be profit making or on issuance of dividends to the shareholders, among others.

[27] This essentially means that while the fund is not authorized, the manager needs to be FINMA licensed.

registered with the Federal Department of Finance as of 12 November 2024.[28] Accordingly, requirements under CISA and CISO that relate to authorization and approval from FINMA (including amendments and changes through the fund life) do not apply. Discussions with market participants indicate that while this product will be attractive, it is not expected to become substantially significant in the Swiss asset management industry.

27. While not authorized, L-QIFs are regulated at a fund level under CISA similar to other funds, with certain exemptions, for instance, on investment conditions, diversification requirements, and prospectus. Open-ended funds are subject to leverage caps through limits on borrowing, pledge of securities, and total exposures.[29] Liquidity risk management requirements apply to open-ended L-QIFs. Special regulations apply to L-QIFs that invest directly in real estate, similar to other real estate funds. L-QIF must set out information on the special features and risks of the individual investments in terms of their characteristics and valuation in the fund contract. L-QIFs are also subject to SRO standards. Some requirements, however, do not apply. For instance, all regulations that relate to authorization or approval from FINMA do not apply. The requirement to prepare a prospectus does not apply. There are no investment conditions in the regulations, which effectively broadens the scope of investment to a wide variety of securities and non-securities (including real estate, crypto, art, wines, etc.). Disclosures of risks associated with such investments, however, apply. Risk diversification requirements do not apply, but related disclosures apply.

28. The fund itself is not directly, but indirectly supervised through the fund manager by FINMA. For instance, the fund manager is subject to requirements relating to risk management and knowledge and experience requirements for staff for such funds, as for other funds. In addition, the newly introduced liquidity risk management requirements continue to apply at the manager level even for such funds. There are reporting obligations, but the reporting is done to the Federal Department of Finance (FDF) rather than to FINMA. All L-QIFs must be notified to the FDF with information on the structure, strategy, and planned asset classes of the fund. Periodic reporting requirements to the FDF are also laid down. The FDF has delegated this reporting requirement to the SNB. SNB collects data from L-QIFs using the same template as for other funds. These include information on the assets, liabilities and risk data including a breakdown of assets and liabilities by maturity and a statement of off-balance-sheet transactions. FINMA receives such information from its information sharing arrangements and plans to incorporate such information in its own supervisory process.

Recommendation

29. FINMA should closely monitor risks from L-QIFs and substitute lower authorization checks with correspondingly higher supervisory intensity, particularly if such funds become a material business of the fund manager. At this point, the supervision of L-QIFs is limited, given that it is at a very nascent stage and only few funds have been formed so far. As the industry grows,

[28] Limited Qualified Investor Funds (L-QIF)

[29] An L-QIF can (i) borrow amounting to a maximum of 50 % of the net fund assets; (ii) pledge or assign as security a maximum of 100 % of the net fund assets; (iii) Overall exposure of no more than 600 % of the net fund assets. Leverage limits are same as applicable to 'other funds for alternative assets' under the CISA Act.

FINMA should monitor risks from such funds from a greater supervisory intensity, given the absence of authorization and therefore, lack of entry-level checks. This should be particularly the case where such funds become a substantial business of a fund manager. Care should also be taken to ensure that, as regulations are expanded for other funds in the future, regulatory arbitrage does not arise between such funds and other similar structures.[30]

E. Liquidity Risk Management for Open-Ended Funds

30. Internationally, there has been increased focus on liquidity risk management of open-ended funds in the last few years which was also reflected in the updates to the CIS regulatory and supervisory framework in Switzerland. FSB issued its recommendations for liquidity risk management for open-ended funds (OEFs) in 2017, followed by IOSCO recommendations in 2018. Crises and stresses resulted in FSB recommendations for money market funds (MMFs) in 2021, a review of the FSB OEF framework and an IOSCO guidance on anti-dilution liquidity management tools in 2023, and IOSCO's consultation on review and update of its own CIS liquidity risk management recommendations (and complementary implementation guidance) in 2024. Further work on the topic is planned[31] In addition, authorities in several jurisdictions updated their own regulatory and supervisory frameworks. In line with these developments, the Swiss regulatory and supervisory framework for liquidity risk management of open-ended funds were also enhanced by amending CISA (CIS Act) and CISO (CIS Ordinance) on the regulatory side (with effect from 2024) and enhancements in authorization, supervision, and reporting on the supervisory side.

31. The regulatory framework under CISO now explicitly specifies liquidity management duties for fund managers. These relate to (i) an appropriate process for the early identification of liquidity risks for each OEF, with certain principles laid down under CISO (e.g., the investment liquidity profile must be consistent with the investment policy and redemption conditions) (ii) ongoing monitoring and assessment of liquidity risks (iii) stress tests at least a year, based on normal and extraordinary market conditions, historical and hypothetical scenarios[32] (iv) crisis plan for every CIS, including use of liquidity management tools, procedures, and internal responsibilities, with an obligation of regular review.

32. CISO now also has provisions relating to liquidity management tools (LMTs). Appropriate LMTs must be provided for an open-ended CIS, depending on the liquidity of the investments, the distribution of risk, the investor base and the redemption frequency. An explicit legal basis has now been created for FINMA to allow the creation of side pockets in exceptional cases, subject to a prior possibility in the fund contract and wider investor interest, at the request of the fund manager. A legal basis for gating was introduced in CISO in 2020. Open-ended real estate funds are subject to a stringent LMT – a 12 month notice period and only effective at the end of the accounting year (many are also listed on the exchange providing another source of liquidity). In

[30] L-QIF are subject to the provisions of the CISA, unless the CISA explicitly provides otherwise, which obviates the risk of regulatory arbitrage, unless a specific exemption is provided. The recommendation above should be read in this context.

[31] Data gaps and a stock-take. (See Enhancing the Resilience of Non-Bank Financial Intermediation: Progress report)

[32] Waived for funds with AUM < CHF 25 million.

practice, Swiss asset managers have a broad set of LMTs at their disposal. Based on information received from the authorities, fund contracts provide for three or more LMTs; almost all Swiss CIS provide for deferred repayment; for MMFs, this is mandatory under self-regulatory standards. Other LMTs include longer redemption and notice periods, redemption gates, redemption fees, swing pricing, anti-dilution levy, temporary borrowing, redemption in kind and side pockets.

33. Regulatory requirements for Money Market Funds (MMFs) were strengthened based on 2021 FSB recommendations. MMFs are a small part of the funds industry in Switzerland (~3.5% of the net fund assets), dominated by a few players. Importantly, constant NAV MMFs are not permitted. Investors are largely retail. A substantial part of the regulation of MMFs is based on self-regulation by the asset management industry association AMAS, which is approved by FINMA.[33] AMAS Guidance on MMFs was amended in 2022 introducing a minimum liquidity threshold of 5%/7.5% for daily maturity in Swiss/ foreign currency respectively. As mentioned above, deferred payment is a mandatory LMT for MMFs under the AMAS Guidance. These structural and regulatory features likely reflected in the fact that MMFs did not face liquidity pressures during 2020.

34. Review of the liquidity management provisions is now a part of the authorization process. For OEFs other than real estate funds, the maximum proportion of potentially illiquid investments permitted by the fund contract is reviewed during authorization. If the figure exceeds a certain threshold, clarification is sought as to how these risks are mitigated on an institutional and on a fund level. If doubts arise as to the compatibility of the potentially illiquid investments, redemption frequency and notice period, FINMA demands clarification from the fund manager, such as plausible stress tests based on different scenarios, model portfolio overview and detailed explanations as to how the fund manager seeks to effectively reduce liquidity risks. If potential liquidity risks cannot be eliminated beyond doubt, FINMA may seek adjustments to the investment policy, redemption frequency, notice period and/ or additional LMTs (which have been employed in practice).

35. Reporting and supervision with respect to OEF liquidity risks has been enhanced. New reporting requirements improved data on portfolio and investor liquidity and available LMTs, enabling FINMA to identify liquidity gaps. Since the last FSAP, FINMA undertook an in-depth analysis on the topic, including substantial off-site and on-site work. The exercise was focused on certain funds deemed to be at high liquidity risk- small and mid-cap equity funds (especially Swiss stocks), CHF fixed income funds, real estate funds, and MMFs. Information was gathered on aspects such as assets liquidity, investor base and behavior, redemption coverage ratio, stress tests parameters and methodology, reverse stress testing, back testing, use of LMTs. FINMA requested stress tests based on predefined parameters. In specific cases, FINMA conducted its own liquidity assessment of the asset side to compare with data provided. Managers not in-line with best practices were challenged and asked to improve their processes. Inflows and outflows at fund and asset class level were monitored to identify trends and potential liquidity issues; dashboards were

[33] AMAS self-regulation currently includes key topics such as MMFs, real estate funds, valuation, among others, and are recognized by the FINMA as a minimum standard. Such recognition by FINMA accords such SRO standards the same regulatory status as regulations issued by FINMA.

developed for the specific fund categories. 22 thematic on-site inspections on the topic were/ are proposed to be conducted between 2022-2024 on the most important fund managers. The increase in supervisory intensity resulted in improved industry practices (e.g., wider implementation of LMTs, more transparency in fund contracts) and awareness. FINMA plans to further develop its own stress test framework and expand it to further investment fund categories. Such a stress test framework will strengthen the current supervisory framework for liquidity risks and should be implemented on priority.

36. Crises since the last FSAP did not significantly affect the Swiss asset management industry, partially likely due to structural and regulatory reasons, although real estate funds continue to face some redemption pressures. OEFs in different parts of the world faced redemption pressures during recent crises (e.g., Covid (2020)/ Russia-Ukraine conflict (2022)). However, FINMA, in its assessment, found no indication of financial stability risks. The structure of the Swiss funds industry is likely to have played an alleviating role- a significant proportion of Swiss funds are aimed at institutional investors; one-third of the total are single-investor funds. Constant NAV MMFs are not permitted. Certain stringent LMTs are required as per law – e.g., a 12 month notice for open-ended real estate funds. Nevertheless, some redemption pressures are observed and continue to persist for certain real estate funds. Swiss real estate funds represent AUM of approx. CHF 77 bn (June 2024). Most invest in Swiss real estate, a very small portion (4%) investing abroad. Redemption requests totaled CHF 1.6 bn. or 2.3% of AUM in 2023/2024; predominant was the share of funds with foreign real estate investments at CHF 0.9 bn. So far, no Swiss real estate fund has deferred its redemptions. Based on FINMA's supervisory analysis, periodic reporting or reviews of annual and interim financial statements were implemented for real estate funds with higher risks.

Recommendations

37. Significant enhancements to the legal and regulatory framework for liquidity risk management of CIS should be continued by implementation of recent FSB and IOSCO recommendations on priority. The 2023 FSB and IOSCO recommendations require long-term regulatory adaptation of Swiss regulatory framework to implement the categorization approach and other liquidity measures. Currently, FINMA and FDF propose to wait till the FSB standards are operationalized into the IOSCO Recommendations and further international guidance on stress tests and valuation are in place, which would effectively mean regulatory work is expected to start post Q2 2025. For several reasons, FINMA and FDF should begin their regulatory impact analysis as soon as possible. Firstly, revision of IOSCO framework is technical in nature and is unlikely to change the fundamental recommendations made by FSB, of which Switzerland is a member. The other related proposed guidance are technical in nature and will only enhance and providing clarity on the existing FSB recommendations. Secondly, FINMA already has been provided the power to regulate the details on the topic, which could obviate the need to adopt a lengthy legislative process for certain aspects. Thirdly, the impact of the revised recommendations is as yet unknown and if the analysis shows a potentially high impact, it is even more imperative for the work to start as soon as possible. At the very minimum, impact assessment should begin as soon as possible.

F. Supervision, Reporting, and Enforcement[34]

38. FINMA introduced a new CIS reporting in 2021. This is a significant enhancement since the last FSAP and in line with recommendations. The reporting is on an annual basis and provides data on liquidity, leverage, exposure, borrowing, collateral, and counterparty risk on a granular level for each fund. The reporting is entirely electronic, using a new platform developed by FINMA. It includes data on all Swiss CIS and foreign CIS with alternative investment strategies managed by a Swiss fund manager (incl. banks or securities firms), both above a CHF 500 mn threshold. This new FINMA CIS Reporting complements the already existing reporting by the Swiss National Bank (SNB) for Swiss CIS whereby data on all Swiss open-ended CIS is collected on a quarterly basis. As part of a cross-divisional data collection, FINMA collected data in 2020 on the AUM in pension schemes and CIS held with insurance companies, banks, and securities firms, which is to be repeated end-2024.

39. FINMA improved its analytical capacity through deployment of new technology. FINMA significantly upgraded its data warehouse (DWH) infrastructure and the created data cubes providing supervisory staff with dashboards that enable in-depth data analysis, risk assessment and comprehensive overviews of the supervised entities. In parallel, FINMA integrated a Business Intelligence (BI) solution within its Asset Management division, specifically targeting the Early Warning and Rating System (FRA). Historically, the early warning system generated automated alerts through algorithms but lacked a user-friendly interface for accessing supervisory data. The newly implemented Power BI solution improves supervisory analytical capability.

40. Post UBS-Credit Suisse merger, FINMA has increased its supervisory intensity of the merged asset management entities. The fund management company and manager of collective assets created out of the merger control quite a large part of all Swiss fund assets, resulting in enhanced concentration risk in an industry which was already concentrated before the merger. The two entities are now in a higher supervision category.[35] FINMA pro-actively determines the audit strategy in coordination with the regulatory auditor. Monthly fund-level quantitative reporting and qualitative quarterly manager-level reporting has been introduced. More frequent on-site inspections and discussions with the board of directors and management have been established. FINMA will now issue an assessment letter at least every two years depending on the rating.

41. FINMA has ramped up its interaction with relevant foreign authorities since 2020. Since 2020, FINMA defined specific circumstances in which exchanges with foreign authorities must occur in its authorization/ approval processes, e.g., establishment of subsidiaries or branches abroad by Swiss supervised institutions (and vice versa), transfer of key personnel, and delegations of critical functions. This has resulted in an average of approximately 120 interactions with foreign regulators per year since 2020, with a noticeable upward trend. For ongoing supervision, FINMA collaborates with foreign regulators on a case-by-case basis under existing MoUs. FINMA is a signatory to IOSCO MMoU and Enhanced MMoU (EMMoU) and has bilateral MoUs with various supervisory authorities.

[34] Since supervision of liquidity risks for open-ended funds is already covered above, it is not repeated here.

[35] All supervised institutions are divided into five supervisory categories based on size and importance, Category 1 being the highest. Further, every institution is assigned a rating based on applicable risks and weights. The category and rating define the intensity and depth of the supervisory instruments and their focus areas.

High-profile cross-border cases, in which various foreign securities regulators were involved, heightened the need for such cooperation. In addition, FINMA holds regular annual meetings with a peer group of supervisory authorities from Luxembourg, Germany, and Liechtenstein, to address broader issues.

42. In 2021, FINMA conducted a thematic surveillance on depository banks. In the previous FSAP, recommendations were made to FINMA to closely monitor the effectiveness of valuation safeguards to address potential conflict of interests within a banking group. The objective of FINMA's exercise in 2021 was to verify that depositary banks follow the rules of proper conduct related to loyalty, diligence, and investor information obligations. The analysis considered both quantitative factors, such as the volume of deposits and intra-group relationships, and qualitative aspects, such as the banks' internal measures and previous audits. Specifically, it sought to confirm that these banks notify investors transparently in cases of conflicts of interest arising from delegated activities. On-site or virtual on-site reviews were carried out at selected banks and desk review was conducted among selected institutions involving a detailed examination of any other delegated activities. Based on submission by FINMA, it is understood that there were no significant concerns.

43. FINMA has also recently enhanced its supervision of greenwashing risks, in the authorization and supervisory processes. In November 2021, FINMA published Guidance 05/2021 with the aim of preventing and combating greenwashing and defining greenwashing in its supervisory framework. During CIS authorization, FINMA ensures that certain sustainability-related disclosure requirements are implemented. These include areas such as naming/ labelling, investment objectives and strategies, risk disclosures, marketing materials and website disclosures, and periodic sustainability related reporting. FINMA has conducted on-site thematic inspections on sustainability at fund managers as well as desk reviews/fund analyses on deception (e.g. based on press/ whistleblowers). FINMA also analyzed the sustainability reporting of all Swiss real estate funds and assessed consistency with the sustainability strategy as described in the fund documents.

44. A recent major enforcement case involved a bank's asset management activity, which resulted in enforcement action by FINMA as well as ongoing criminal proceedings. FINMA deployed remedial measures and required governance and risk management arrangements. Enforcement proceedings against the relevant individuals have been initiated. Criminal proceedings are pending. The case highlighted significant potential impact of the asset management business on a bank, including reputational risks as well as potential impact on the bank balance sheet.

Recommendations

45. Reporting requirements should be enhanced, particularly with respect to foreign CIS, cross-sectoral data, early warning events, and overall periodicity. FINMA should upgrade its reporting system with respect to the following:

- Data relating to foreign CIS is currently limited, both in terms of foreign CIS managed by Swiss fund managers and foreign CIS marketed to Swiss investors. For foreign CIS managed by Swiss fund managers, reporting is limited to CIS with AUM more than 500 million and for alternative strategies. Further, apart from number of total foreign CIS marketed to Swiss retail investors, no

other data is available. For non-retail funds, even the number is not available. This limits supervisory visibility over potential areas of systemic concern or investor protection in the CIS not covered in the reporting. At the very minimum, high-level data should be available for an aggregated picture, with granularity considered for specific risks, as applicable.

- Cross-sectoral data of CIS held with banks, securities firms, and insurance companies is collected currently on an ad hoc basis, which should be regularized. Reporting formats should be made uniform for similar activities irrespective of the type of license enabling a holistic view.

- FINMA does not have reporting of early warning events, for instance, redemptions over a certain threshold, significant valuation write-downs, use of ex-post LMTs, etc. Event-based reporting should be introduced both for domestic and foreign CIS to enable FINMA to detect early potential systemic risks.

- The overall periodicity of granular reporting to FINMA is only annual. The data reporting to SNB does not have the granularity of FINMA reporting. While the new reporting is a significant improvement since the last FSAP, as the next step, periodicity should be improved, at least for high-risk funds/ fund managers and/or in high-risk areas.

46. Cross-sectoral supervision of asset management activities should be introduced within FINMA. Currently, asset management activities of only fund management companies, manager of collective assets and portfolio managers are supervised by the asset management division. Supervision of asset management activities of banks, securities firms, and insurance companies are not handled by the asset management division and reside within respective divisions. While the asset management division is usually consulted with respect to supervision of such entities, the arrangement overall results in a fragmentation of supervision and a differential approach across FINMA for similar activities. The proposed reorganization of FINMA is expected to make asset management division more cross-sectoral. Given that the licensing approach permits multiple types of entities to conduct similar activities under different licenses, a more activity-based approach than an entity-based approach should be adopted within the organization structure to ensure harmonization in supervisory approach and practice. This will also highlight gaps in the licensing, regulatory and supervisory processes, for harmonization across various licenses. The authorities have informed that they are already considering such an initiative. FINMA should implement this initiative sooner rather than later to ensure consistency across the organization.

47. Fund manager-custodian bank relationships should be subject to more intensive supervision in the risk framework. Given the dominance of banks in the asset management industry in Switzerland, fund manager-bank relationships assume significance. Custodian banks have significant obligations under the CISA, not just limited to custody but also extending to oversight functions, particularly with respect to NAV calculation, compliance of investment decisions with the law, etc. While there are independence provisions in the regulatory framework with respect to management/ executives, whether these have been sufficient in practice to obviate the inherent conflicts of interest should be regularly tested through the supervisory process. Based on the previous FSAP recommendation, a recent thematic surveillance by FINMA on custodian banks assessed compliance with rules of conduct with respect to loyalty, diligence, and investor disclosures

of conflicts of interest, while focusing on the NAV function. This is an encouraging initiative. However, on a more structural form, assigning a higher risk in the supervisory framework for such relationships could result in a fundamentally intensive supervisory process for both the fund managers and the depository activities.

48. FINMA should publish its supervisory expectations to provide clarity on implementation and supervision. With a principle-based regulatory approach, it becomes important to provide clarity on supervisory expectations for effective implementation of such principles. In practice, this need not take the form of a one-size-fits-all expectations but can be a holistic multi-approach framework, even based on a comply-or-explain principle to retain the regulatory intent to provide flexibility in implementation. Lack of publicly available supervisory expectations simply creates a vacuum that provides clarity neither to the industry (on how to implement the rules), nor to the supervisors (on how to monitor and confirm the implementation of the rules), given that in Switzerland's context, this includes not only FINMA but also other entities such as regulatory auditors, supervisory organizations, and SROs. In practice, today FINMA issues such expectations only to the relevant entities that are the subjects of on-site/off-site supervision; there is no visibility to the rest of the industry. FINMA is currently limited in its ability to publicly lay down such supervisory expectations, which is often seen as a form of regulation for which FINMA has a limited role. In the past, this also resulted in some such supervisory expectations being withdrawn, affecting credibility of the institution itself. FINMA should publish its supervisory expectations and any legal impediment for it to do so should be effectively removed.[36]

49. The supervisory ratings process should be subject to regular review based on outcomes. The supervisory process, particularly for Category 3-5 entities currently rely primarily on ratings to determine scope and intensity of supervision. This rating further depends on a number of risks included within the framework and weights assigned to those risks. This dependency on the rating system requires regular and deep review of the outcomes of the rating system to ensure that it is fit for purpose. For instance, the current supervisory ratings system classifies a significantly large portion of the portfolio managers as high-risk entities, which should necessitate a review of the selection of underlying risks, the risk weights, and the overall rating system for its effectiveness.

50. Resources should be enhanced for supervision of asset and wealth management activities, particularly of banks. While there has been an increase in the resourcing for asset management division, there is a need for further enhancement given the sheer size and expanse of the industry. In particular, the resources allocation to non-prudential/ conduct supervision of wealth management and asset management activities of banks is not enough considering the size of such activities and their importance to bank revenues and profits. As banks shift their focus to more of such activities, the risk-taking is also likely to shift in that direction which needs more supervisory intensity from FINMA for the purpose. Consequently, FINMA should enhance its resources for supervision of asset management and wealth management activities, particularly of banks. FINMA

[36] Please refer to the discussion in the Detailed Assessment Report for Basel Core Principles (principle 1) for a deeper discussion on the topic.

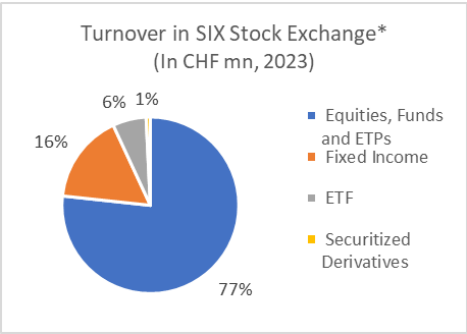
should increase its direct supervision of such activities and limit reliance on auditors to compliance-based audits.

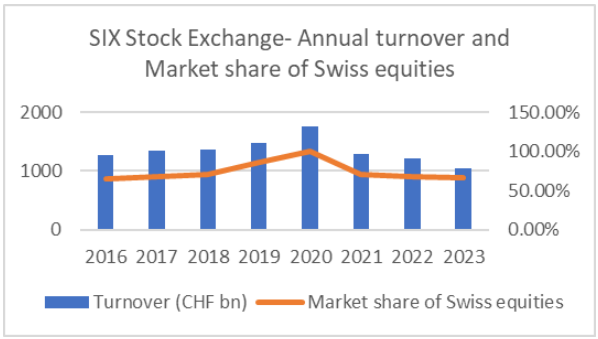
TRADING SYSTEMS

A. Industry Overview

51. Securities trading in Switzerland is concentrated in one stock exchange. 99.99% of the turnover of on-venue trading in Switzerland is done on SIX Securities Exchange (SSX). SSX is a part of the larger SIX Group which operates almost the entire financial market infrastructure in the country including the payments systems as well as securities settlement and depository. SIX Group also operates a digital stock exchange under the SIX group umbrella (elaborated later) as well as other smaller businesses. SIX is owned primarily by banks, of which one bank owns a significant part of the total shareholding of the exchange. Apart from SIX, there is another stock exchange operating in the country called BX Swiss which was acquired by Börse Stuttgart GmbH (a Germany-based group then operating in Germany and Netherlands) in 2018. BX Swiss has turnover of less than 0.01% of the total on-venue turnover in Switzerland, and unlike SIX which focuses on institutional investors, BX Swiss has products listed and traded aimed towards retail investors. Apart from stock exchanges, there are certain Organized Trading Facilities (mainly by banks) which operate securities trading on a discretionary or bilateral basis or have trading platforms for non-securities.

Figure 1. Switzerland: Trading in SIX Stock Exchange





* Securitized derivatives include structured products and warrants. Exchange Traded Products (ETPs) include crypto products. Equities constitute the bulk of trading under the section equities, funds, and ETPs.

52. Bulk of securities trading is in domestic equities. Issuers are largely domestic.[37] SIX Swiss Exchange is the reference market for Swiss securities and home to over 250 Swiss stocks, including some of Europe's most important blue chips. The total market capitalization is CHF 1.7 trillion (2023), of which top 10 issuers constitute 92%. Swiss equities are primarily traded in SIX and UK trading venues with SIX leading the market share. Apart from equities, other products traded on SIX exchange include bonds, structured products, Exchange Traded Funds (ETFs), Exchange Traded Products (ETPs), and Investment Funds. Trading in ETFs and bonds constitute 16% and 6% of the total turnover on SSX respectively. SIX market share in Swiss equities increased to almost 100% in

[37] Bx Swiss has admitted equities of several foreign issuers for trading, but the turnover is minimal

2020 after the EU equivalence decision, which then shrank after recognition was granted to UK venues (See Box 1 for more details).

Box 1. Switzerland: Impact of EU Equivalence Decision on Securities Trading

In 2019, a decision by the EU Commission not to extend equivalence to Switzerland had a significant impact on trading of shares in Switzerland. The EU Markets in Financial Instruments Directive (MiFID II) and the EU Markets in Financial Instruments Regulation (MiFIR) were implemented in January 2018. Article 23 MiFIR introduced a so-called share trading obligation, which required EU banks and investment firms to trade certain shares on an EU trading venue or a recognized third country venue[1]. A prerequisite for recognition of a third country venue is an assessment by the EU Commission of its market integrity and transparency regulations as EU equivalent. In December 2017, the EU Commission conducted an assessment and recognized regulation of Swiss trading venues as equivalent for a period of one year, with extension dependent on development on ongoing political negotiations on an institutional agreement, (broader in nature than trading venue regulation)[2]. However, by Nov 2018, the extension was not granted which effectively meant a prohibition on EU investment firms to trade Swiss shares in Switzerland.

As a consequence, the Swiss Federal Government adopted emergency protective measures in Nov 2018 to prevent shift of trading of Swiss shares on EU trading venues. This was implemented by way of an Ordinance which introduced, since January 2019, the requirement of prior FINMA-recognition of foreign trading venues, if they admit or enable trading of equity securities of Swiss companies (provided the securities are already listed/admitted to trading on a Swiss trading venue). A precondition for such recognition is that the foreign trading venue shall not be domiciled in a jurisdiction that restricts its market participants from trading equity securities of Swiss companies on Swiss trading venues, according to an FDF list. After the recognition of equivalence by the European Commission expired on June 30, 2019, the FDF added the EU and its member states to the list of relevant jurisdictions, thus activating the emergency measures vis-à-vis those jurisdictions. This shifted the trading in Swiss shares almost entirely to the SIX exchange. Swiss equity securities were now no longer subject to the share trading obligation (since due to the emergency measures, significant portion of global trading volume was not inside the EU) and EU investment firms traded Swiss equity securities on Swiss trading venues (primarily SIX). In Jan 2024, these emergency measures were merged into FinMIA (Art. 41a *et seq*.)).

On January 29, 2025, the protective measures were lifted, and the Swiss Federal Council decided to remove the EU from the list of jurisdictions with effect as of May 1, 2025. This followed a recent amendment to EU MiFIR in 2024, based on which the trading obligation is now limited to shares with an EEA ISIN; significant trading in the EU is no longer a prerequisite for the trading obligation; and exemption from the trading obligation is granted to shares traded on a third-country venue in the local currency or in a non-EEA currency. Accordingly, while the EU still does not recognize Swiss stock exchanges as equivalent, Swiss Shares are no longer subject to the share trading obligations under MiFIR. This will again allow dual listings of Swiss companies in the EU and ends the de facto ban on dual listings which had been in place since 2019.

This series of events highlighted the potential for cross-border risks to significantly affect the secondary markets in Switzerland. The impact of larger political decisions on equity trading in Switzerland was significant. Historically, around 30% of Swiss equities were traded on EU-based venues (pre-Brexit mainly UK based MTFs)[3]. The risk of significant liquidity in Swiss trading venues migrating to these EU venues was quickly limited by the protective measures. More than 300 Swiss shares were delisted from the EU-based exchanges and multilateral trading facilities (MTFs). The trading in Swiss shares effectively moved primarily to the SIX exchange.[4] Post-Brexit, once the UK agreed to recognize Swiss trading venues as equivalent, recognition was granted to UK trading venues in February 2021, resulting in some move of this liquidity to UK trading venues.[5] In summary, some legal maneuvering in response to the potential materialization of the risk appears to have resulted in Switzerland benefiting from the outcome of the events in this case, but this may not always be possible. Overall, these events exposed the cross-border vulnerabilities of Swiss secondary markets, especially as a large part of the trading volume continues to created by foreign members.

Box 1. Switzerland: Impact of EU Equivalence Decision on Securities Trading (Concluded)

[1] The obligation applied to shares which were already significantly traded on an EU exchange or Multilateral Trading Facility.

[2] Implementing decision - 2017/2441 - EN - EUR-Lex (europa.eu); MiFID II: Commission adopts equivalence decision on Swiss share trading venues (europa.eu)

[3] The only game in town - The TRADE (thetradenews.com)

[4] The SIX primary exchange saw a significant increase in share from 37% in June 2019 to 50.9% the following month. Some flows also moved to Systematic Internalisers and OTC market in EU since the ban only applied to trading in exchanges and Multilateral Trading Venues. SwissAtMid, SIX Swiss Exchange's dark venue also gained share significantly, increasing from around 40% of the dark market in Swiss equities to almost all of it post the decision. (Source: ibid)

[5] Market share of venues for Swiss-listed equities as on September 2024 (YTD excl. off-venue volumes): SIX Swiss Exchange (CH) 70.8%, Cboe Europe (UK MTF) 19.2%, Aquis (UK MTF) 5.0%, Turquoise (UK MTF) 2.5%, Other MTFs 2.5%

B. Legal Framework

53. Trading systems are regulated primarily under the Federal Act on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading (FinMIA) and related Ordinance FinMIO. FinMIA was introduced in 2015 in response to the global developments since the Global Financial Crisis in 2008 and subsequent reforms with respect to OTC derivatives trading. The provisions then scattered across the Stock Exchange Act, the Banking Act and the National Bank Act were repealed and a single law governing financial market infrastructure and market conduct in securities and derivatives trading was created with provisions adapted to the changing conditions. It is primarily based on the EU law at that point of time, albeit with some modifications.

54. Since the last FSAP, FinMIA was significantly amended to permit a new type of license for DLT Trading systems; further substantial reforms have been proposed in June 2024. In 2021, the new DLT trading systems license was introduced under FinMIA as a part of a holistic set of legislative amendments brought about to permit and bring clarity on issuance, holding, and trading of DLT securities in Switzerland (See Box 2 for more details). In addition, as a part of the five-year review post introduction of FinMIA, significant reforms have been proposed in June 2024 which pertain, inter-alia, to areas such as market abuse (dealt within the respective topics under this Section).

C. Licensing Framework

55. There are four types of trading systems under FinMIA- stock exchanges, multilateral trading facilities (MTFs), DLT trading facilities, and organized trading facilities (OTFs). FINMA has the authority to grant licenses for these trading systems.[38] Stock exchanges and MTFs are collectively referred to as 'trading venues'. Both stock exchanges and MTFs are institutions for multilateral trading of securities based on non-discretionary rules, the key difference being that apart from trading, stock exchanges can also undertake listing of securities. A DLT trading license also permits operation of a non-discretionary multilateral trading platform but is unique in two areas – firstly, it permits both trading and post-trading functions under the same license; secondly, it

[38] An OTF is operated under an existing license, e.g. by a bank or a securities firm, as explained later in the para.

permits direct access to individuals and unregulated entities to the trading platform (both not permitted under the more traditional trading venue licenses).[39] OTFs resemble a residual bucket which include trading systems for securities on a bilateral basis or based on discretionary rules and trading systems for non-securities.[40] OTFs can only be operated by banks, securities firms, trading venues or DLT trading facilities, and as such do not need a separate OTF license from FINMA. While FinMIA largely reflects EU rules, it is important to note that OTFs in the Swiss context includes both OTFs and parts of the Systematic Internalizers (SIs) [41] in the EU context. Trading venues are not designated as systemically important FMIs (which then also involves the role of Swiss National Bank).[42]

56. At present, there are 3 stock exchanges and 1 MTF licensed by FINMA- all part of the SIX group, except the stock exchange BX Swiss AG. SIX group operates two stock exchanges- the SIX Securities Exchange (SSX) for traditional securities and SIX Digital Exchange (SDX) with a focus on Distributed Ledger Technology (DLT)-based securities. It also operates an MTF called SIX Repo AG for multi-currency repo and money market instruments.[43] BX Swiss is another stock exchange in the country, albeit with very low volumes compared to SSX.[44] No DLT trading facility has been licensed so far, although there are applications under process. Post Eurex Zurich ceasing operations in 2018, there is no trading venue for derivatives in Switzerland anymore. Some banks and securities firms operate OTFs in the country, however, data on trading in OTFs is not available.

57. FinMIA and FinMIO lay down detailed licensing requirements for trading venues and DLT Trading Systems; requirements for OTFs are governed by FinMIA, FinMIO, and a FINMA circular. The requirements for trading venues (stock exchanges and MTFs) primarily relate to the legal entity, place of management, organization and governance, self-regulatory functions, outsourcing, fitness and propriety, compliance and risk management, minimum capital, business continuity, IT systems, and orderly trading. FINMA may require an applicant to produce an auditor report of fulfillment of authorization conditions. Requirements for DLT Trading Facilities are similar to that of trading venues, with certain additional requirements but relaxations on proportionality considerations (See Box 2 above). The operation of an OTF does not require a separate license but must be reported to FINMA by the supervised entity. Upon receipt of the notification, FINMA checks compliance with legal requirements laid down in FinMIA and FinMIO, which are further specified in a

[39] DLT trading facilities cannot list securities, but this is expected to be permitted in the future based on the proposed FinMIA reforms.

[40] Multilateral trading in securities based on non-discretionary rules is only possible on an MTF or stock exchange.

[41] Put simply, a Systematic Internaliser (SI) is a European Union regulatory classification for investment firms that, on a frequent, systematic, and substantial basis, execute client orders on their own account.

[42] A DLT Trading Facility can be a systemically important FMI, although limited to post-trading functions under the license.

[43] In the case of SIX Repo, only the segment 'OTC secondary spot market' is subject to FINMA supervision *(includes trading in SNB bills / GMBF (money market instruments)* Segments operated in cooperation with SNB and inter-bank repo market (not securities) are excluded from FINMA supervision.

[44] BX Swiss was operating as a "stock exchange – like" institution under FINMA license since 1999 and was granted a stock exchange authorization in 2017 post introduction of FinMIA.

FINMA circular .[45] The requirements for OTFs are relaxed compared to that for trading venues in several areas including trading rules and market abuse.[46]

Box 2. Switzerland: Distributed Ledger Technology (DLT)-Based Securities Trading[1]

In August 2021, Switzerland became one of the first countries to enact explicit laws for use of distributed ledger technology (DLT), which also apply to DLT based securities trading. The Act did not fundamentally overhaul the existing legal framework but selectively adapted ten existing federal laws, the overall purpose being to foster innovation and develop Switzerland as a leading location for blockchain/DLT companies. The Swiss Code of Obligations now has a new category of 'ledger-based securities'[2] thereby providing a high level of legal certainty for issuance and transfer of rights on distributed ledgers.

A new licensing framework for 'DLT Trading Facility' was introduced under FinMIA, focused on trading exclusively in DLT based securities. This framework is similar to the framework for traditional trading venues with two key additional aspects which are permitted for such facilities but not for traditional venues: (i) the license permits both trading and post-trading functions (clearing, settlement, custody) under the same license, (ii) retail investors and unregulated entities can directly be participants. Certain additional requirements apply, for instance, relating to clearing and settlement functions similar to CSDs, as well as those relating to the nature of the technology (audit of smart contracts and the ledger). On the other hand, to encourage innovation, proportionality relaxations are also available for small DLT trading facilities.[3]

SIX group launched a digital exchange (SDX) in 2021 for trading in DLT securities; the platform has mainly been used for listing of bonds and trading is limited. SDX enables atomic settlement based on the underlying technology. However, with the interoperability with the traditional SIX stock exchange system, trading currently happens on the traditional stock exchange rather than the new platform. It is also key to note that SDX operates under a traditional stock exchange and CSD license (as two separate entities) rather than the new DLT Trading Facility license. In March 2025, FINMA licensed BX Digital AG, a sister company of the BX Swiss AG, as the first DLT trading facility.

FINMA should continue to monitor trading in DLT-based securities and review its supervisory framework for sufficiency to deal with new risks from such trading. In case of any move from atomic settlement to delayed settlement, FINMA should consider a re-assessment of potential settlement risks.[4] Direct participation of retail investors poses additional conduct-related risks, which need to be carefully assessed. Conduct of non-regulated activities within the same legal entity could also pose risks to the regulated activities. These risks come in the backdrop of a new technology that is yet not fully tested and is prone to unexpected risks. FINMA should build up its expertise on the new technology and review its supervisory framework for sufficiency to deal with these additional risks.

[1] This Note focuses on the regulatory and supervisory framework relating to DLT Trading Facilities. The broader framework for FinTech and tokenized assets are dealt in the Technical Notes on FinTech and FMIs (second mission).

[2] The provisions do not mention DLT or blockchain, but the background papers for the Act and the register characteristics in the Law make it clear that the legislator had DLT in mind while formulating it.

[3] These include relaxations with respect to independence of the self-regulation functions, internal audit, and business continuity. While differential regulatory provisions which arise from the nature of the new technology are understandable, relaxations for smaller venues which do not exist for the traditional licenses, raise questions on the tech neutrality of the licensing and regulatory regime.

[4] Based on industry discussions during the mission.

[45] FINMA Circular 2018/1 Organised trading facilities

[46] The organization requirements to prevent market abuse under the relevant circular (FINMA-Circular 13/08) do not apply to OTFs.

58. Material changes post authorization require formal application and FINMA approval, while non-essential changes only need to be notified.[47] For regulations of trading venues and DLT trading facilities, all amendments require FINMA approval, regardless of whether they are essential or not. Amendments to processes (e.g., listing, admission to trading, membership, access) require FINMA notification or approval, depending on the materiality.

Recommendations

59. FINMA should closely monitor trading outside regulated venues in the country, especially in OTFs. Trading in Swiss equities has been shifting from on-venue trades to off-venue trades over the last five years. While UK venues are expected to be constituting a significant portion, it is as yet unclear what proportion of this trading is happening within Switzerland. FINMA does not have data on trading in OTFs; focus so far has been primarily on trading venues. FINMA should seek regular reporting on trading data from existing OTFs. In addition, if analysis of trading data exhibits trading on systems in Switzerland which have not been registered as OTFs, necessary clarifications must be sought, and appropriate action must be taken. In addition to monitoring of trades within the country, FINMA should also consider monitoring, at a high-level, trading in Swiss securities globally, in order to analyze trends in potential cross-border risks as well as liquidity and price formation risks.

60. The regulatory and supervisory requirements and processes with respect to OTFs should be reviewed and suitably enhanced in areas of high risk. FINMA circular for OTF (2018/1) currently lays down high level principles with respect to trading rules and duties of the OTF operator. The requirements are much relaxed compared to trading venues, although many risks are similar. In some cases, the risks are potentially higher for an OTF due to its features -e.g., discretionary basis for trading, bilateral trading, and direct participants. The statutory prohibitions against market abuse do not apply to securities solely traded on an OTF. Hence, notwithstanding the responsibility imposed on OTFs to ensure orderly trading, surveillance obligations with respect to market abuse do not apply to OTFs, despite thinner volumes (prone to market manipulation) and direct participation (lack of controls for insider trading). There are no issuer related obligations, despite potential for risky issuers to be admitted to trading. The supervision of OTFs is currently done by the banking division which views risks from a banking rather than a markets perspective, resulting in a lack of adequate supervision from a markets perspective. Overall, FINMA should improve its monitoring and supervision of OTFs, and if areas of high risk are systematically observed, should consider taking up with the FDF the need for necessary regulatory improvements. For such monitoring and supervision, FINMA should review its current organization structure and enable a cross-functional structure that enables a market-wide view for supervision of OTFs, in addition to the current entity-level view.

D. Role of SROs

61. Trading venues must create SROs under FinMIA. FinMIA is flexible in its approach on how the trading venue should structure the SRO. It only stipulates that trading venues should establish

[47] As far as they relate to aspects which are of relevance in the context of the authorization.

an SRO appropriate for its activity. In practice, this has resulted in SIX group establishing SIX Exchange Regulation AG ("SER") as a separate legal entity for fulfilling SRO functions for all its trading venues (including SDX and SIX Repo). For BX Swiss, however, this is done structurally by establishing a separate functional department within the same legal entity. FinMIA does not provide for a separate authorization for the SROs but covers it under overall supervision of the trading venue, the relevant outsourcing arrangement and consolidated supervision of the overall group, as applicable. There are certain independence provisions with respect to the SRO, including approval of key persons by FINMA. Provisions for DLT Trading facilities are similar to those for trading venues, with the exception of some relaxations for smaller trading venues. OTFs do not have to create an SRO.[48] While the requirements on system resilience, orderly trading and pre-trade transparency for OTFs are similar to trading venues, the market control and surveillance function of an OTF are subject to less granular requirements.

62. SROs almost entirely regulate, supervise, and enforce, aspects relating to trading (including surveillance), participants, and issuers. For instance, within SER, the Regulatory Board undertakes the regulatory functions and approves regulations for issuers and participants. The Issuer Committee has a specific role to decide on applications for listing and admission to trading and has representatives of both issuers and investors. SER undertakes monitoring and supervisory functions such as monitoring of participants and issuers and undertaking trade surveillance, primarily for detecting market abuse cases. Exchanges currently rely primarily on audits for supervision of participants; issuer supervision is primarily focused on review of periodic disclosure obligations. Quasi-judicial bodies enforce SRO rules and include a Sanctions Commission, Independent Appeals Board and Board of Arbitration. Similar groups/ boards exist within BX Swiss as well to fulfil various SRO functions. Enforcement powers include powers to fine, delist issuers, suspend participants, halt trading, among others. While listing and admission to trading is governed by the SRO under FinMIA, the prospectus review function is carried out separately as a 'prospectus office' under FinSA. Both SER and BX Swiss exchange are authorized as prospectus offices under FinSA. In addition, BX Swiss also acts as a 'client adviser register' under FinSA for client advisers (see asset management section above).

63. FINMA supervises SROs and collaborates with the SROs with respect to market surveillance for market abuse. For issuers, the regulatory, supervisory and enforcement functions almost entirely lie with the SROs. Similar is the case with prospectus office. Substantial part of the rules and regulations applicable to activities of participants are laid down by the SRO, which also supervises and enforces such rules and regulations.[49] FINMA's role is mainly exercised through supervision of the SROs themselves. In case of market surveillance, the surveillance function is currently done by the exchanges. FINMA receives details of potential market abuse cases from the exchange SRO, investigates and enforces it, often in collaboration with the Attorney General office.

[48] FINMA's OTF circular sets out principles regarding the scope and content of an OTF's rules which must be transparent.

[49] At a broader level, FINMA (or corresponding foreign authority) continue(s) to be the prudential supervisor of the participants, which are mostly banks.

However, based on the discussions during the mission, it is understood that the cooperation and collaboration between FINMA and the SROs has been challenging, as explained in the later section.

E. Pre- and Post-Trade Transparency

64. The regulations provide for post-trade transparency for all securities. Under FinMIA, the trading venue is required to immediately publish information on the transactions carried out on the trading venue and on the transactions conducted outside of the trading venue reported to it for all securities admitted to trading. In particular, the price, volume and time of the transactions must be published. The same requirements apply to DLT trading facilities.

65. The legal framework currently provides for pre-trade transparency for shares, but not for other securities. FinMIA requires that trading venues shall publish in real time the bid and offer prices as well as the sizes of the trading positions at these prices for shares. An enabling provision exists to apply these to securities other than shares under FinMIO which has not yet been exercised. The same pre-trade transparency provisions apply to DLT trading facilities as to trading venues. Under FinMIO, pre-trade transparency obligations that apply to trading venues apply by reference to OTFs for both multilateral and bilateral trading where a liquid market exists (also only for equities similar to trading venues). SROs also have certain specific provisions relating to pre-trade transparency in their trading rules, but are limited currently to trading in shares, in line with the larger regulatory framework.

66. The regulatory framework provides for certain exemptions from pre-trade transparency requirements. A trading venue may make provision for pre-trade transparency exceptions in its regulations for (i) reference price systems, as long as the reference prices are widely published and viewed by participants as reliable (ii) systems that exist only to formalize transactions already negotiated (iii) orders held in an order management facility of the trading venue pending disclosure (iv) orders that are large in scale compared with normal market size. Such regulation and any amendments to it are subject to FINMA's prior approval. There is no price improvement requirement for dark trading. In addition, securities transactions are not subject to the provisions on pre-trade transparency if they are carried out as part of public tasks and not for investment purposes. Similar exemptions apply in case of DLT trading facilities. These exemptions also apply to OTFs, but only where multilateral trading takes place. Where OTFs operate matched principal trading, no allowance may be made for exceptions from the transparency provisions.

67. SSX has had a large dark pool called SwissAtMid since 2016 that uses the pre-trade transparency exemption for reference prices. It allows for execution of Swiss equity trades at the midpoint of the Swiss Stock Exchange's lit order book. It is primarily a venue for participants looking for block liquidity in Swiss shares. Other pre-trade transparency exemptions are used by SSX for certain specific types of orders. Overall, around 5.56% of trades in SSX constitutes dark trading. Given the lack of data on OTF trading activities, it is unclear what part of the trades in OTFs constitute dark trading.

Recommendations

68. Pre-trade transparency requirements for trading in non-equity securities should be considered. FInMIA already envisages and provides for such a requirement. The stated intent at that point of time (2015) of introduction at a later stage was to wait till related requirements at the EU level are in force.[50] Today, there is sufficient experience of applying pre-trade transparency requirements on non-equity securities at the international level. There is already significant trading in non-equity instruments at SIX Stock Exchange. With additional market monitoring of trading outside trading venues, more trading in non-equity securities may come to light. With this context, pre-trade transparency should be considered for non-equity securities through suitable revisions to the regulatory framework.

F. Market Abuse

69. Provisions pertaining to market abuse are mainly found in FinMIA and FInMIO, with certain organization requirements for supervised institutions mentioned under a FINMA circular. FinMIA lays down broad definitions of insider information, insider trading, and market manipulation and has prohibitory provisions. Exploitation of insider information and price manipulation are also criminal offences under FinMIA, which then further lays down respective conditions and punishments. Currently, the provisions under FinMIA mainly apply to trading venues and DLT trading facilities; a broad provision on market abuse exists under the OTF circular. The trading venues also have their own rules and regulations related to market conduct that apply within their own regulatory and supervisory domain (e.g., for participants). In addition to potential sanctions, the trading rules also provide for the cancellation or rejection of such trades. Under FINMA circular 2013/8, supervised institutions such as banks, securities firms and asset managers have certain organizational requirements to prevent and deal with market abuse, where usually off-the-shelf systems are used.

70. The obligation for surveillance for market abuse primarily lies with the trading venues. The obligation also extends to review of the transactions conducted outside of the trading venue that are reported to it or are brought to its attention in any other way. SIX previously relied on an external provider but has since developed its own in-house surveillance system. In addition to surveillance by trading venues, supervised institutions (e.g., banks) also have the obligation to report detected suspicions that are of substantial importance to FINMA under FINMASA. FINMA at present has no major role in surveillance and its functions are mainly limited to investigating and enforcing cases brought to its attention by trading venues and through other sources. FINMA can conduct own analysis in its investigation and can request information such as beneficial owner information, further trade and order information, etc. mainly from the respective banks, securities firms, trading venues and other involved parties (e.g., issuers, market participants).

71. FINMA closely collaborates with the Office of Attorney General (OAG) for investigation and enforcement of market abuse cases. Cases flagged and forwarded to OAG are usually those

[50] Explanatory Report on the Ordinance on Financial Market Infrastructures and Market Conduct in Securities and Derivatives Trading, 2015

which are criminal offences, relating to entities which are not directly supervised by FINMA (e.g., issuers, natural persons), or where FINMA does not have sufficient investigative tools to gather evidence such as recording phones, search and seizure, etc. FINMA relies on a higher level of evidence for enforcing insider trading cases, which often translates to involvement of Attorney General office for use of their investigative powers to gather evidence.

72. Market abuse cases require close collaboration between several institutions domestically as well as cross-border in some cases. For surveillance purposes, SIX Swiss Exchange and BX Swiss have an agreement in place to regularly exchange trading data on a case-by-case basis in compliance with the related regulatory requirement under FinMIA. For investigation and enforcement, FINMA, Attorney General's Office, Takeover Board, and trading supervisory body of the trading venue regularly exchange relevant information. Where cases are cross-border, the IOSCO MMoU and EMMoU are the primary instruments used by FINMA, while in some cases bilateral MoUs with certain countries could also be used. In the 2014 assessment, IMF had recommended that in case of requests from foreign supervisors, prior intimation to, and agreement of the concerned individual before fulfilling the request should be done away with.[51] Since then, legal amendments have permitted FINMA to exceptionally refrain from prior intimation to the client if the foreign authority substantiates the request that in doing so, the purpose of the request will be compromised. Subsequent intimation is still required when the risk ceases to exist, and the concerned individual client can ask the court to review the transmission's lawfulness. FINMA has widely used this delayed notification process for market abuse cases. A proposal completely to do away with client notification or make a general exception for market abuse cases is under consideration, which if implemented, which will be in line with the 2014 recommendations.

73. FINMA has conducted enforcement proceedings in several cases, while referring many to the Office of Attorney General ("OAG"). In the past five years, FINMA conducted 11 enforcement proceedings enforcing the market abuse provisions. These proceedings led to declaratory rulings, bans from practicing a profession, bans of a dealer from conducting business and confiscation of illegal gains. FINMA also referred 36 cases with regard to market abuse to OAG (mostly suspicions on insider trading) and issued 18 letters of reprimand to market participants.

74. Recently proposed FinMIA reforms (under public consultation in 2024), if implemented and well-executed, could result in substantial improvements in preventing, detecting, and enforcing market abuse cases. Changes proposed under the reforms include four key aspects relevant to market abuse: (i) Transfer of issuer obligations of ad hoc publicity and management transaction (transaction by key executives in own shares) disclosures from self-regulation to State law as well as further strengthening (e.g., requirement to publish name and function of the person for management transactions, obligation to maintain insider lists) (ii) FINMA to undertake the main market surveillance, including for cross-market abuses (complementing exchange SRO surveillance functions) based on transaction reports, and for this purpose,

[51] In addition to the obvious risk of compromising the investigation, if the client does not agree, he also can challenge the transmission before court, which is time consuming and can delay the transmission for several months.

centralization of reporting office under FINMA.[52] (iii) Lowering the threshold for supervised entities to intimate FINMA from suspected cases of substantial importance to simply a suspicion of market abuse ("suspicious transaction reports"), similar to corresponding EU requirements.[53] This is expected to enable better detection of more substantiated market abuse cases. (iv) Enhancing criminal enforcement of market abuse cases though expanding the scope of price manipulation transactions as criminal offences, enhancing punishment for tertiary insiders, reducing financial thresholds for offences to qualify as serious (criminal) market abuse cases, and use of improved technology for investigation.[54]

75. The current framework of collaboration between FINMA and exchange SROs for market abuse related functions suffers from serious deficiencies. The IOSCO standards allow delegation of supervisory functions to SROs. However, a key element for the effectiveness of such framework is a high level of collaboration between the supervisor and the SRO. In the Swiss context, discussions indicate a sub-optimal level of collaboration between the two institutions, particularly on market abuse. Key Questions for assessment of IOSCO Principle 9 relating to SROs include: *(i) Does the legislation or the regulator require the SRO to demonstrate that it cooperates with the regulator and other domestic SROs to investigate and enforce applicable laws, regulations and rules (ii) Does the SRO have MoUs or other arrangements in place to secure cooperation between it and the regulator? (iii) Does the regulator have in place an effective ongoing oversight program of the SRO, which includes review and revocation of SRO governing laws, regulations, and rules? (iv) Does the regulator retain full authority to inquire into matters affecting the investors or the market? (v) Does the regulator take over or support an SRO's responsibilities where the powers of an SRO are inadequate for inquiring into or addressing particular misconduct or allegations of misconduct or where a conflict of interest necessitates it?* The current legislative and regulatory framework under FinMIA and FinMIO requires cooperation between the SRO and the regulator only in limited areas (e.g., market supervision) and no MoUs between the SROs and FINMA have been implemented. FINMA also does not have the power to require exchange SROs to change the SRO laws/regulations/rules (after the initial approval process), for instance, based on supervisory findings. FINMA does not have the power to take over SRO responsibilities, for instance, where conflicts of interest necessitate it. These indicate significant gaps in the legal, regulatory and supervisory framework with respect to such SROs. Market manipulation cases from Swiss Trading Venues to FINMA account only for roughly 2% of all market abuse cases, which reflect the lack of effective outcomes out of surveillance, especially regarding market manipulation. The reforms that propose to centralize surveillance and related reporting functions within FINMA and the related recommendations that follow in the next para should be seen in this context.

[52] The explanations for the reforms indicate that this is being proposed due to the fragmentation of the reporting system and the resulting differences in data quality. This will also result in no need for a reporting office at the SRO level. Quality of the transaction reports, key to detect market abuse, is also expected to be enhanced.

[53] Discussions indicate that while the proposed suspicious transaction reporting will resemble EU requirements, the threshold may still be slightly higher to not result in a significant volume of unnecessary reporting that is difficult to sift through. That being said, the threshold will still be lower than what currently exists in Switzerland.

[54] Tertiary insiders who now can only be punished with a fine will not be abolished and merged into secondary insiders which have more serious consequences.

Recommendations

76. Explicit SRO-FINMA cooperation obligations should be introduced under law and greater power should be accorded to FINMA over SROs in line with above IOSCO requirements. An explicit MoU between the trading venue SROs and FINMA detailing specific areas and procedures for cooperation could provide another layer of foundation to the cooperation framework. FINMA's oversight powers should include review and revocation of SRO governing laws, regulations, and rules. FINMA should have full authority to inquire into matters affecting the investors or the market and to take over SRO's responsibilities in case conflicts of interest necessitate it. Such requirements should be introduced even if surveillance functions and reporting are centralized within FINMA (as proposed in the recent market abuse reforms) - even in such cases, trading venues will continue to play a key role in detection, investigation, and enforcement of market abuse cases.

77. The proposed reforms that strengthen prevention, detection, and enforcement of market abuse should be implemented on priority. The proposed reforms, if implemented and properly executed, have the potential to significantly enhance the current market abuse regime. Lowering of reporting thresholds for market abuse cases for supervised institutions is key to detection of such cases and should be implemented on priority. Disclosure of beneficial ownership details are also key in detecting market abuse cases, and the proposed requirements should be implemented.[55] Centralizing reporting and surveillance function within FINMA, as is currently proposed in the reforms, could be an effective alternative in the context of the current level of suboptimal cooperation and collaboration between the exchange SROs and FINMA. This will necessitate significant investments in technology and human resources within FINMA, which should be suitably allocated, in case such a reform is implemented. Implementation of the recommendations on legal provisions for cooperation and enhanced powers for FINMA over SROs will continue to be relevant.

78. Regulatory and supervisory requirements to ensure sufficient mechanisms and controls to prevent insider trading should be enhanced at the level of issuers and supervised institutions. A preliminary examination of a sample of insider trading cases highlighted basic insider trading offences, which indicate lack of adequate controls at the level of issuers who own the information and supervised institutions who execute the trades. With respect to issuers, the current self-regulatory requirements by exchange SROs are high-level and do not require adequate controls to prevent insider trading. At the supervised entity level, FINMA also lays down high level requirements for such entities to prevent market abuse. At both the levels, requirements should be enhanced to be more granular and specific, whether by laying down supervisory expectations or regulatory requirements, as appropriate.

79. Market surveillance of market manipulation must be improved to ensure sufficient detection of such cases. In 2024, only nearly 11% of cases received by FINMA pertain to market manipulation. Based on the data and type of cases enforced, it appears likely that many such cases

[55] Such information should also enable the trading venues and FINMA to monitor large exposures for systemic risk purposes at a beneficial ownership level (see IOSCO principle 37).

are going undetected, whether due to lack of quality data or adequate surveillance capability, or both. In cooperation with the exchanges, FINMA should undertake a review of potential reasons for lack of adequate market manipulation cases and suitable measures should be implemented to address the issue.

80. Investigation and enforcement of market abuse cases should be improved, through improved investigation and enforcement tools with FINMA. The threshold to transfer cases to the OAG as criminal should be high and limited to serious cases. At present, cases are being transferred to OAG due to either lack of adequate investigation powers (e.g., lack of powers to obtain telephone records, search and seizure powers) or lack of sufficient enforcement powers (e.g., powers to fine individuals and companies). This results in cases being converted to criminal cases where administrative enforcement may have been sufficient raising questions of proportionality. In addition, criminal cases have a higher threshold of evidence which results in additional difficulty in enforcement of such cases. FINMA should be given clear enforcement powers, at least the power to fine individuals and companies for market abuse cases, enabling it to have a complete and proportionate toolkit depending on the offence. Further, FINMA should have the investigation powers such as search and seizure, powers to obtain telephone records, etc., at the very minimum on a case-by-case basis on approval from the OAG, for administrative enforcement of market abuse cases. Further, FINMA currently has, due to judicial decisions in the past, a rather high threshold for circumstantial evidence for proceeding with enforcement of insider trading cases, which coupled with lack of investigative tools mentioned above, hinders its ability to enforce sophisticated insider trading cases. In case FINMA is of the opinion that such judicial pronouncements consistently hinder its ability to enforce insider trading cases, it should use those as evidence to seek relevant powers from the legislator for this purpose.

G. Market Resilience and Integrity

81. Market resilience is key for Switzerland given the concentration of trading in one venue and the importance of that venue for trading in Swiss equities. As outlined earlier in the section, SIX Stock Exchange dominates securities trading in the country. Globally, SIX Stock Exchange is the leading stock exchange for Swiss equities, leading to several venues and providers depending on SIX for reference prices for these stocks. Apart from the trading activity, in the context of larger SIX group, it is key to note that the group practically manages the entire financial market infrastructure in the country, whereby any cracks in the infrastructure could have severe consequences to the country's financial system. Several parts of the IT system are shared across the group, which also exposes the trading systems to risks coming from activities beyond pure trading.

82. SIX Swiss Exchange (SSX) suffered two major trading outages since the last FSAP- in June 2023 and July 2024. In June 2023, there was an outage for three hours, which was the worst outage for the exchange since 2012, on account of a technical glitch. In July 2024, trading was suspended across all segments for four hours before resuming, primarily due to a data issue. This also accordingly affected trading in certain foreign venues reliant on market data feed from SSX. SSX is not unique in suffering trading outages in recent years; similar outages have been experienced across venues globally. That being said, concentration of trading and dependencies raise a higher level of resilience risk in case of Switzerland than other countries where alternatives are available.

Multiple outages have sparked a renewed focus from regulators globally on outages resulting in IOSCO publishing good practices in case of trading outages in June 2024.[56] In August 2024, SIX Swiss Exchange published its Emergency and Outage Principles laying down its broad policy and procedures for outages. The incidents were reported to FINMA and followed up with detailed discussions in the course of the supervisory process, resulting in improvements to address the weaknesses exposed by the outages and further follow-up measures.

83. Operational resilience and outsourcing requirements apply under the regulatory and supervisory framework.[57] FINMA recently issued a circular (2023/1) providing for requirements relating to operational risks and resilience, which includes provisions relating to resilience, reliability, and integrity of critical systems. While not directly applicable to FMIs, these currently apply to the SIX group through a separate notification. Broad outsourcing requirements apply under FinMIA and FinMIO, primarily relating to outsourcing of essential services. Such outsourcing of essential services is subject to FINMA's prior approval and certain substantive requirements apply (e.g., minimum content of the outsourcing agreement, risk management, audit rights). FINMA Circular 2018/3 which lays down supervisory expectations with respect to outsourcing also does not directly apply to FMIs but the relevant provisions of FinMIA and FinMIO are interpreted accordingly.

84. Given concentration risks in trading combined with lack of domestic alternatives, operational and market resilience are of high supervisory priority. Dominance of a single trading venue, concentration of trading, and dependencies for reference prices exposes the country's trading systems to significant concerns of market resilience. While cross-border trading is possible, at a domestic level, there are practically no alternatives. Trading outages in the recent years have exposed vulnerabilities in reliance on one trading system. Given these risks, FINMA has accorded and should continue to accord a greater priority in its supervisory process for market and operational resilience. Operational risk and IT have been rated as the highest risks in FINMA's last supervisory rating. FINMA has performed supervisory reviews, external audits, raised specific assessment letter points, established ad hoc interventions/measures for critical incidents and have further measures in the pipeline in this area. Nevertheless, there is scope for further improvements, particular in the area of cyber risks, as outlined in greater detail in the TN on Cyber risks on this topic.

85. Ex-ante and ex-post controls exist to maintain orderly trading. Ex-post tools at the level of trading venues include power to suspend/halt trading, impose circuit breakers, suspend trading participants in case of exceeding trading volumes in certain instruments, terminate participants/ suspend access to the system, deletion of orders, cancellation of trades, among others. Most of these aspects are governed through self-regulation, while some are required under law (e.g., power to halt trading in extraordinary circumstances). Ex-ante tools also exist, for instance, controls concerning Direct Electronic Access, etc. Default procedures exist in case of default of contracting parties at a trade level (e.g., buy-in obligations on the seller) as well as at the level of the clearing

[56] FR04/2024 Market Outages

[57] These issues and related recommendations are covered in detail in a separate Technical Note on cyber risks as well as in the broader technical note on FMIs (second mission). To avoid redundancy, this technical note does not delve into details of these aspects.

member (e.g., default funds, waterfall procedure, segregation, and portability). Trading in shares, ETFs, CHF bonds and certain ETPs are centrally cleared by SIX x-clear AG, the Swiss cash CCP and LCH & CBoE Clear in interoperability; related risk management requirements and procedures apply. For instruments that are not centrally cleared (e.g., structured products), volumes are very small. While most tools are implemented by the trading venues, FINMA also has the power to order the reduction of a large position or the provision of additional margin during its ongoing supervision of market participants. Should a supervised institution not implement the requested corrective measures, the issue can be escalated to enforcement.

86. Trading participants are subject to flagging and reporting requirements for algorithmic and high frequency trading. Under FinMIO, the trading venue must be able to identify the orders generated by algorithmic trading, the different algorithms used for the creation of orders; and the participants' dealers who initiated these orders in the trading facility. The trading venue shall require participants that pursue algorithmic trading to flag such orders, record all entered orders, including order cancellations. The participants should possess effective precautions and risk controls that ensure that their systems are robust and equipped with sufficient capacity to deal with peak volumes of orders and announcements, are subject to appropriate trading thresholds and upper limits, do not cause or contribute to any disruptions in the trading venue, are effective to prevent market abuse. The participant systems should also subject to appropriate tests of algorithms and control mechanisms, including precautions to limit the proportion of unexecuted trading orders relative to the number of transactions that can be entered into the system by a participant, slow down the flow of orders if there is a risk of the capacity of the system being reached, and limit and enforce the minimum tick size that may be executed on the trading venue. In order to take account of the additional burden on system capacity, the trading venue is also permitted to make provision for higher fees for certain types of orders (especially cancellations) and participants. Provisions which impose obligations on participants to flag algo trades and identify algorithms are also included in the SRO regulations. SER's participant audit also covers these provisions.

87. There are no restrictions on short selling; the framework focuses on reduction of settlement fails. Neither FinMIA nor FinMIO contain any restrictions on short-selling. FinMIO permits a trading venue to impose a duty on participants to flag short-sales but in practice, this has not been implemented. On the other hand, a more explicit rule on short sellings was deleted from the SSX regulations around 2012. Under the current trading rules of the SSX, the only requirement applicable to short selling is that members must ensure performance of their obligation (settlement) occurs on the contractual due date. BX Swiss AG has no rules in place regarding short selling. Since there is no requirement to flag short-sales, there is no clear data available either with the trading venue or with FINMA on short selling. Focus is rather on minimizing settlement fails through settlement discipline regimes, buy-in rules, and related monitoring. Based on CSD data available with FINMA, FINMA is of the opinion that settlement fails are low and not of systemic concern. Under special circumstances, SIX has the power to issue regulations on short-selling, designed as an emergency measure, subject to notification to the participants. This has not been used so far.

88. Market liquidity is shifting towards off-venue trades and less transparent execution mechanisms (e.g., dark trading and auctions). Discussions with the industry indicate that liquidity

in Swiss securities is moving outside the traditional trading venues, which is also in line with the global trend.[58] In on-book volumes, dark pools, closing and periodic auctions, and other alternative closing methods enjoy increasing relevance, especially observed by foreign MTFs. As there is a reduced transparency in these mechanisms, this raise concerns due to the reduction of volumes in price-forming lit markets. Liquidity fragmentation is another concern, albeit primarily cross-border. Industry discussions also confirmed these trading patterns (e.g. dark trading) in Swiss equities, but primarily in venues outside Switzerland, albeit due to lack of data of off-venue trading in Switzerland, this cannot be fully confirmed.

Recommendations

89. FINMA should closely monitor trading activities that may significantly affect price discovery and market efficiency on a systematic basis. This includes areas such as on-venue vs off-venue trading, dark trading, reference price venues, liquidity fragmentation, concentration in auctions, among others. While substantial trading in Swiss equities happen outside Switzerland, close monitoring of trends, even at a high level, will help FINMA monitor related risks to market efficiency and integrity. FINMA should also closely monitor such trends from a market resilience perspective since events such as outages where liquidity is concentrated, or the reference price of the primary exchange is of substantial importance and therefore could have serious ramifications on market functioning.

90. FINMA should obtain information on and monitor short selling. Currently, the trading systems do not involve flagging of short sales, although FinMIO permits trading venues to do so. IOSCO recommends a reporting regime that provides timely short selling information to the market or, as a minimum requirement, to market authorities. Although FINMA has indicated that data from CSD highlights low settlement fails, at the very minimum, ability to identify short selling activities and monitoring of such activities should be incorporated in the trading or trade reporting systems and FINMA's supervisory regime.

H. Supervision and Enforcement

91. The trading venues as well as the SROs are required to provide periodic reports and ad-hoc substantial incidental reports to FINMA. The extent of the periodic reports is risk based and is slightly different for each supervised entity. Key reports include financial reports, strategy plans, risk dashboard, risk appetite statement, and internal audit reports. The SRO is also required to periodically submit reports to FINMA by exchange regulation. The responsible FINMA staff member reviews each report. Risks identified in the reports are discussed in subsequent supervisory meetings or addressed immediately if severe. In addition to the agreed reporting, the supervised entities must also immediately report any incident of substantial supervisory importance to FINMA.

92. The approach to define the priorities for off-site and on-site inspections are described in the FINMA internal supervisory concept for FMIs. This concept currently covers the supervision of the trading venues on an individual level as well as a part of the consolidated

[58] As per FINMA, more than 50% of trading volume currently occurs off-book.

supervision at a group level.[59] Processes for on-site reviews (supervisory reviews & deep dives) are defined and outlined in an appendix to the internal supervisory concept.

93. Entity/group-level categorization (primarily based on size) and risk-based ratings together determine the supervisory approach. Across FINMA, all supervised institutions (including FMIs and their groups) are divided into five supervisory categories, based on the institution's size and importance for the Swiss financial market. In additional to categorization, similar to other supervised institutions, FMIs are also annually rated on certain risk criteria based on the ongoing supervision by FINMA and regulatory auditors. The category and rating together define the supervisory scope and depth. For instance, on-site inspections for FMI groups are conducted by FINMA two to four times per year, while for smaller FMI institutions (without consolidated supervision), every 2-3 years. Standard supervisory instruments include regular supervisory meetings with management and technical experts, on-site reviews, annual audits by the audit firm, and for the first two categories - an annual assessment letter from FINMA including supervisory focus points and deadlines for mitigation. Besides the standard instruments, case-based clarifications are carried out as needed (e.g., trading outages).

94. On-site inspections are carried out either as broader supervisory reviews (SR) or topic specific deep dives (DD). These take roughly three days and one day respectively. This can cover the whole group or specific subsidiaries (e.g. trading venues and their SROs), depending on the risk assessment. The topics covered are risk-based and can cover changes of the supervised institution, e.g. organizational changes, new businesses areas, identified weaknesses, regulatory changes, and areas which have not been assessed by FINMA for a longer period. For instance, in the last five years, SRs have included areas such as operational risk, market surveillance, fire-drill cyber exercise, exchange regulation, listing, data management, outsourcing, business continuity management, corporate governance, etc. Similarly, DDs have included areas such as cyber risk, issuer disclosures, project management, IT risk management framework, etc. Some of these have translated to initiation of investigations against the trading venues/ SROs but have not resulted in enforcement actions in the last five years.

95. Regulatory audit done by audit firms is a very important part of supervisory process at FINMA, including for trading systems. A standard audit strategy is applied for supervised institutions in FINMA Supervisory Categories 3 to 5. The calculated net risk exposure in each audit field will determine the audit periodicity and audit depth. For supervised institutions in FINMA Supervisory Categories 1 and 2, FINMA exerts greater influence on the audit areas to be covered by defining an audit strategy in dialogue with the audit firm. Once an audit firm has completed a regulatory audit, it communicates the findings to FINMA in the form of a standardized report. The report contains the audit firm's opinion on compliance with the stipulated requirements and all irregularities which have been identified or on recommendations for improvements.

96. Given the cross-border activities of the trading venues, FINMA closely cooperates with foreign supervisors in its supervisory process. Apart from trading operations in Switzerland, SIX group also operates the Spanish BME trading operations. BX Swiss is part of the German Börse

[59] FINMA supervises OTFs through the respective license, e.g., the banking license.

Stuttgart group, which operates in Germany, Switzerland, the Netherlands, and the Nordics. Trading in Swiss equities involves cross-border activities including trading on foreign venues, by foreign participants, and investors. All of these necessitate cross-border cooperation with foreign regulators. FINMA is a signatory to the IOSCO MMoU and since October 2019, to the IOSCO Enhanced MMoU (Annex A.2) which allows FINMA to cooperate with foreign regulators on supervision and enforcement. FINMA cooperates with foreign regulators where trading venues have cross-country operations, for instance, through joint on-site audits. Specific to trading venues, FINMA also has bilateral cooperation agreements with UK FSA (now FCA) since 2011 for the supervision and oversight of SIX Swiss Exchange (Recognized Overseas Investment Exchange in the UK) and with China Securities Regulatory Commission (CSRC) since 2022 on the market regulation of the China-Switzerland Stock Connect.

Recommendations

97. FINMA should enhance supervision of the trading venue SROs. Trading venue SROs have a wide range of substantial regulatory, supervisory and enforcement functions, as mentioned earlier. Past on-site inspections have covered various functions of the SROs on an individual function basis, but the periodicity and the scope does not appear to be sufficient to cover the wide-ranging SRO functions of the trading venues. The frequency and intensity of supervision of trading venue SROs should be increased. This, in addition to other supervisory improvements, will involve deployment of additional resources, which the markets division and related enforcement division under FINMA currently lacks. In addition, concentration of stakeholders in the governance of SRO functions of the trading venues (including shareholders, participants, and issuers) exposes SRO functions to significant risks regarding independence and conflicts of interest. SROs should be subject to additional supervisory intensity in terms of potential outcomes resulting from conflicts of interest. Regulatory reform could also be considered if the resultant outcomes suggest difficulties in mitigation of conflicts within the current framework and related need for regulatory reforms.

98. Issuer-related functions of SROs should be subject to increased supervision. Issuer related regulations of the SRO are currently high-level and principle-based and its implementation by issuers is at present unclear. Issuer related functions of SRO were subject to on-site review in the recent past, but need greater intensity and frequency of supervision, particularly a review of implementation of these self-regulatory requirements and the effectiveness of the current enforcement regime. This should cover not only aspects such as ad-hoc and periodical disclosure obligations of issuers but also obligations pertaining to market abuse.

99. The effectiveness of the current licensing, regulatory and supervisory framework for prospectus office functions should be reviewed and based on the outcome, suitable reforms to the legislative framework should be introduced. FinSA introduced the concept of prospectus offices entrusting such bodies with the task of checking that the prospectuses are complete, coherent and understandable.[60] The Swiss regulatory framework for prospectus review is unique given the lack of review of the contents of the prospectus for accuracy by the prospectus office;

[60] Prior to FinSA, prospectuses were subject to fragmented regulation and the breach of their obligations by issuers already resulted in an almost systematic sanction.

focus being primarily on completeness. Further, the regulatory framework provides for post-facto rather than a prior review of the prospectus for non-equity securities. The effectiveness of this regime, particularly in areas such as misstatements in prospectus is currently untested. The current legislative framework accords FINMA a limited role with respect to such offices: the licensing power, receipt of a yearly report, and limited supervisory powers (limited to intervention in cases where the office does not fulfil its requirements and is no longer able to perform its tasks properly). The effectiveness of the current licensing, regulatory and supervisory framework for prospective office functions should be reviewed and based on the outcome, suitable reforms to the legislative framework should be introduced.