



## Swiss bond trading report 2018

The evolution of bond markets and  
an outside-in view on Swiss investors

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custody clients to make holdings information available to the Algomi's bond network. Network members will be able to query those holdings, which will alert the custody holder and give them the ability to trade on the request.<sup>42</sup> The idea of mining data to give market participants a view into the location of every single bond has the potential to unfold a pool of liquidity that could possibly have a big impact.

The likely winner in the race to effectively utilise data are the market participants that do not only use the right analytical technology to detect and aggregate liquidity, but that also have the required order execution technologies in place to transform orders into trades. Therefore, it is important that market participants actively adopt technologies in order to find liquidity in the required scale and to trade this liquidity in the appropriate place. Fact is, bond markets are evolving and so are the underlying technological innovations. It seems unquestionable that the future of bond markets is not the traditional status quo in which investors are solely connected to a set of dealers, but rather in a market organisation where all market participants are interconnected and where technology is key to detect and trade liquidity.

## 1.4 Environment: The regulatory framework for Swiss market participants

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### 1.4.1 Regulation of bond trading: Setting the scene

The following chapter will provide an overview of the key regulatory requirements for trading professionally in securities in the form of a bond in Switzerland.

A bond in the form of a «security» in the sense of Art. 2 para. 1 lit. b FinfraG/FMIA<sup>43</sup> is offered at uniform conditions to multiple parties.<sup>44</sup> Securities are, in other words, standardised, certificated and uncertificated financial instruments suitable for mass trading. They are thus either offered publicly in a similar structure and denomination or placed with more than 20 clients, unless they are being created specifically for individual counterparties.<sup>45</sup>

A security in the form of a bond can trigger multiple legal consequences when being traded. These consequences are:

- Persons professionally trading in securities will potentially have to apply for a licence as a securities dealer (the Swiss equivalent of an investment firm or broker/dealer).
- Facilities allowing for the multilateral trading of securities require a licence as a stock exchange or multilateral trading facility (MTF).
- Facilities allowing for the bilateral trading of securities must be operated by a duly licensed operator (the Swiss bilateral version of an OTF,

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[https://www.bnymellon.com/us/en/\\_locale-assets/pdf/news/at-a-glance-corporate-fact-sheet.pdf](https://www.bnymellon.com/us/en/_locale-assets/pdf/news/at-a-glance-corporate-fact-sheet.pdf)

<sup>42</sup> Source: <http://www.algomi.com/company-news/bnymellon-and-hsbc-team-up-with-algomi>

<sup>43</sup> Swiss Financial Market Infrastructure Act (FinfraG/FMIA).

<sup>44</sup> Art. 1157 para. 1 Swiss Code of Obligations.

<sup>45</sup> Art. 2 para. 1 Swiss Financial Market Ordinance (FinfraV/FMIO).

which replaces the Systematic Internaliser in the EU).

- The public offering of securities requires a prospectus. The listing of securities on a trading venue (stock exchange and MTF) also requires the filing of a listing application and the creation of an accompanying prospectus.

#### 1.4.2 Regulation of investment firms trading bonds pre-FinSA

##### *Swiss-based securities dealers*

Professional trading in securities in the form of bonds typically requires a licence as a securities dealer granted by the Swiss Financial Market Supervisory Authority FINMA. The detailed requirements and licensing process depends heavily upon the place of domicile of the securities dealer and the type of business activity pursued. A Swiss-domiciled securities dealer is any legal entity or partnership that professionally<sup>46</sup> sells or buys securities in the form of bonds either

- on its own account on the secondary market with the intent of reselling them within a short period of time (own account dealers and market makers), or
- for the account of third parties (client dealers), or
- publicly offers securities in the form of bonds to the public on the primary market (issuing houses).<sup>47</sup>

Own account dealers and issuing houses have to be primarily active, on an individual and group-consolidated level, in the financial sector. This means that the main business activity of a group must be in the financial sector. Even sizeable

securities trading activities of treasury companies within a group that is pursuing a primary business purpose other than a financial activity are thus not subject to the licensing requirements of a securities dealer if the securities trading is closely related to the group's business activity.<sup>48</sup> This does not, however, apply to market makers and client dealers that will have to apply for a license even if the group's main business activity is not a financial activity.

##### *Trading on one's own account (proprietary trading)*

Securities dealers trading on their own account with bonds will only have to apply for a license if they pose a systematic risk to the financial system. That is why their gross annual turnover in securities such as bonds must achieve at least CHF 5 billion.<sup>49</sup> They typically do not have any clients. Securities dealers trading on their own account generally act in a professional capacity and on a short-term basis. Key aspects of trading on one's own account include trading without instructions from third parties and taking on risk, which is primarily market risk. In the context of a clearing situation it can, however, lead to a counterparty risk if clients do not advance money to settle the securities.<sup>50</sup> Trading on a short-term basis means the active management of securities to achieve gains from short-term fluctuations in prices or interest rates within a short period of time. Long-term investments in securities in the form of bonds and in particular the holding of securities in the form of bonds until maturity are not deemed to be trading on one's own account.

##### *Trading on one's own account (market makers)*

Market makers trade securities in the form of bonds publicly, in a professional capacity, on their

<sup>46</sup> Meaning any separate and independent economic activity that is designed to achieve regular revenues (see FINMA-Circular 2008/5 Securities Dealer, chiff. 129).

<sup>47</sup> Art. 2 lit. d Stock Exchange and Securities Trader Act (SESTA) in combination with Art. 2 and 3 Swiss Stock

Exchange and Securities Trader Ordinance (SESTO).

<sup>48</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 8 et seq.

<sup>49</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 23.

<sup>50</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 21.

own account and on a short-term basis. They trade publicly, because they offer the securities to anybody. They set a firm bid and ask for prices on an ongoing basis or on request (request for quote).<sup>51</sup>

#### *Trading on behalf of third parties (client trading)*

Client dealers handle securities in the form of bonds in their own name, but on behalf of clients, in their professional capacity. A professional capacity is already assumed if the securities dealer maintains accounts directly or indirectly or acts as a custodian for more than 20 clients.<sup>52</sup> Whether the securities dealer is dealing on the client's account or on his/her own account is determined based on economic considerations, namely who is bearing the risk of the transaction. In the case where the client is bearing the economic risk, trading activities over the nostro accounts of the securities dealer are deemed transactions on behalf of the client.<sup>53</sup> Client dealers maintain accounts for the settlement of the transactions for these clients or with third parties, or keep these securities for themselves or for third parties in their own name.<sup>54</sup>

No licensing requirement is triggered if the entity only deals with clients who are Swiss or foreign banks or securities dealers, other enterprises under government supervision, shareholders or companies with significant holdings in the debtor and any parties affiliated or related to them, and institutional investors with professional treasury departments. Asset managers and investment advisors are not deemed to be securities dealer if they are acting based on a power of attorney, unless they purchase or sell securities to their clients using their own account or securities deposits.<sup>55</sup>

#### *Issuing bonds as securities (issuing houses)*

Securities dealers in the form of issuing houses underwrite bonds issued by third parties on a professional basis at a fixed price or for a commission and offer them to the public on the primary market.<sup>56</sup> A key criteria to decide whether the underwriting and placement of bonds in the primary market is the activity of a securities dealer is thus, whether it is «public». An offering is public if it is addressed to an unlimited number of persons, in particular by means of advertisements in the media, prospectuses or other electronic means. Offers of securities made exclusively to qualified investors such as domestic and foreign banks and securities dealers or other enterprises under government supervision, shareholders and partners with a significant equity interest in the borrower and parties affiliated and related to them, and institutional investors with professional treasury departments, meaning the employment of one person on a full time basis managing the company's assets, are not considered.<sup>57</sup> An offering is deemed to be «public» even if bonds have been placed with fewer than 20 people, but the offering has been addressed to an unlimited number of people not being exclusively qualified investors.<sup>58</sup>

#### *Foreign securities dealers*

Foreign securities dealers are entities that either

- possess an equivalent licence abroad, or
- apply the expression «securities dealer» or an expression of similar meaning in their corporate name, business purpose, or documents, or
- conduct trading in securities as defined in Art. 2 lit. d SESTA.

Foreign securities dealers, meaning entities that

<sup>51</sup> Art. 3 para. 4 SESTO.

<sup>52</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 49.

<sup>53</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 50.

<sup>54</sup> Art. 3 para. 5 SESTO.

<sup>55</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 52.

<sup>56</sup> Art. 3 para. 2 SESTO.

<sup>57</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 14 et seq.

<sup>58</sup> Art. 4 SESTO.

are not domiciled in Switzerland, are generally subject to the same requirements as Swiss-domiciled securities dealers, unless the law sets forth different obligations.<sup>59</sup> Securities dealers that are factually managed in Switzerland and execute their transactions mainly out of Switzerland must incorporate in Switzerland and be organised according to Swiss regulations. They will be subject to the regulatory requirements of a Swiss securities dealer.<sup>60</sup> Securities dealers organised under Swiss law are deemed to be under foreign control if a foreign person indirectly or directly holds more than 50 percent of the votes or has in any other way a material influence on the securities dealer.<sup>61</sup>

Foreign securities dealers will need to be licensed in Switzerland either as a branch or as a representation office if they employ staff in a professional capacity in Switzerland on an ongoing basis.

#### *Branch*

Foreign securities dealers will need to be licensed as a branch of a foreign securities dealer in Switzerland if they trade securities, have client accounts, or legally oblige the foreign securities dealer.<sup>62</sup>

#### *Representation office*

The securities dealer will need to be licensed as a representation office of a foreign securities dealer if it becomes active in any other way in Switzerland, namely by forwarding client orders or performing representational activities.<sup>63</sup> According to established FINMA practice, the following activities are typical of a foreign securities dealer:<sup>64</sup>

- Employing persons in Switzerland that are fully integrated into the organisation and brokering securities trades and forward orders.
- A corporation in Switzerland that is not licensed as a Swiss securities dealer, but carries the same or a similar name and brokers securities and forwards orders.
- Existence of exclusive contracts with natural persons and legal entities in Switzerland to broker securities. The Swiss representative acts in such a situation exclusively for the foreign securities dealer and gets reimbursed for each trade.
- Conclusion of non-exclusive contracts with natural persons and legal entities in Switzerland for the brokering of trades, but authorisation to use its own corporate name. The representative is compensated for each trade.

#### *Member of a Swiss trading venue*

Non-Swiss-domiciled members of a Swiss trading venue such as SIX Swiss Exchange or the multilateral trading facility SIX Corporate Bonds must be approved by FINMA prior to becoming a member of such a trading venue as a «foreign participant to a Swiss trading venue».<sup>65</sup>

#### *Swiss asset managers*

Swiss based asset managers are licensed by FINMA if they are managing collective investment schemes.<sup>66</sup> They ensure proper conduct of portfolio and risk management for one or more collective investment schemes. They might also be entitled to perform additional activities, such as the discretionary management of individual portfolios.<sup>67</sup> They are however not entitled to engage in a securities dealer activity. Any such activity requires an additional license as securities

<sup>59</sup> Art. 40 SESTO.

<sup>60</sup> Art. 38 para. 2 SESTO.

<sup>61</sup> Art. 56 SESTO.

<sup>62</sup> Art. 39 para. 1 lit. a chiff. 1 SESTO.

<sup>63</sup> Art. 39 para. 1 lit. a chiff. 2 SESTO.

<sup>64</sup> FINMA-Circular 2008/5 Securities Dealer, chiff. 54 et seq.

<sup>65</sup> Art. 40 FMIA.

<sup>66</sup> Art. 18 Swiss Collective Investment Schemes Act (CISA).

<sup>67</sup> Art. 18a para. 3 CISA.

dealer. A duly licensed securities dealer does not, however, require an additional license as an asset manager of collective investment schemes.<sup>68</sup> Swiss based asset managers, however, have the duty to carefully select counterparties for securities trades and other transactions. They must offer a guarantee of best execution in terms of price, time and quantity. The choice of counterparties must be reviewed at regular intervals.<sup>69</sup>

Asset managers solely managing individual portfolios are currently not obliged to apply for a license with FINMA. They are, however, subject to duties under the Swiss anti-money-laundering regulation and must register with a self-regulatory organisation.

#### *Obligations of a securities dealer*

##### *Requesting a licence*

Anyone falling within one of the categories of a securities dealer mentioned above has to apply for a licence with the Swiss Financial Market Supervisory Authority FINMA. The licence will be granted if certain key requirements are fulfilled at the time the licence is granted and on an ongoing basis.

##### *Organisational requirements*

A securities dealer must have an adequate organisation in place that allows for the execution of its activities. The securities dealer must have a board of directors and management. The members of the management have to be fit and proper for the execution of their respective function. There must be an adequate separation between trading, asset management and administration.<sup>70</sup> The securities dealer must also

establish an internal control system consisting of compliance, risk management and internal audit.<sup>71</sup> An external regulatory audit firm must also be appointed. It is possible to unify some of the control functions with a specific person.

##### *Capital requirements*

Any securities dealer must have a fully paid-in minimal capital amount of at least CHF 1.5 million. Any shareholder indirectly or directly holding more than 10 percent of the capital or the voting rights of a securities dealer or that may in any other way influence the business activities of the securities dealer must pass the fit and proper test of FINMA.<sup>72</sup> The provisions applicable to banks regarding own capital and accounting generally also apply to a securities dealer.<sup>73</sup> Privileged deposits of clients are subject to enhanced protection.<sup>74</sup>

##### *Reporting, information and approval obligations*

Any securities dealer will have to comply with multiple reporting, information and approval obligations on an ongoing basis. Any change to the preconditions for granting the licence, but in particular the articles of association, regulations, material change of business activity, management, board of directors and external audit firm, as well as build ups, investments and divestments of foreign operations must be pre-approved by FINMA.<sup>75</sup>

Any indirect or direct acquisition or sale of a stake in a securities dealer reaching, exceeding, or falling below the thresholds of 20 percent, 33 percent or 50 percent of the capital or the votes must be reported to FINMA.<sup>76</sup>

Securities dealers have to report any orders and transactions in securities as well as derivatives that

<sup>68</sup> Art. 8a Swiss Collective Investment Schemes Ordinance (CISO).

<sup>69</sup> Art. 22 CISA.

<sup>70</sup> Art. 19 SESTO.

<sup>71</sup> Art. 20 SESTO.

<sup>72</sup> Art. 23 SESTO.

<sup>73</sup> Art. 29 para. 1 SESTO in combination with the Capital Adequacy Ordinance and the Banking Ordinance.

<sup>74</sup> Art. 29a SESTO.

<sup>75</sup> Art. 25 SESTO.

<sup>76</sup> Art. 28 SESTO.

are being derived from securities listed on a Swiss trading venue.<sup>77</sup> Such reporting must be made to the corresponding trading venue.<sup>78</sup>

#### *Algorithmic and high frequency trading*

Participants in Swiss trading venues that are engaging in algorithmic or high frequency trading activities are subject to enhanced recording requirements and their systems must ensure adequate functioning even in stress situations.<sup>79</sup>

#### *Direct electronic market access*

A securities dealer being a member at SIX Swiss Exchange may grant clients direct access to the exchange. The participant remains liable to the exchange for all actions and non-actions on the part of such clients.<sup>80</sup>

#### *Latest Fintech developments regarding securities dealers*

The Swiss Banking Ordinance has recently been amended effective as of August 1, 2017 to better accommodate Fintech entities. Client accounts that are solely used for the settlement of client business within 60 days are thus not deemed to be client deposits potentially triggering the requirement of getting licensed as a bank. The settlement period has thus been extended from the prior 7 days to 60 days. However, this change applies only to banks, but not securities dealers, for whom the current FINMA practice still applies, which does not set forth a particular deadline, but a case-by-case approach.

#### 1.4.3 Regulation of investment firms trading bonds under the FinSA- and FinIA-regime

##### *Bond trading and execution under the FinSA-regime*

Securities will fall within the scope of application of FinSA, because they are assets, meaning financial instruments and other financial investments, in the sense of FinSA.<sup>81</sup> Trading in securities and the execution of client orders related to trading on one's own account in securities in the form of bonds is a financial service.<sup>82</sup> These activities can thus generally only be executed by duly licensed financial intermediaries.

##### *Behavioural requirements*

FinSA sets forth new behavioural requirements for financial market participants. Some of these obligations have already been applied under prior applicable regulations. Others have already been applicable under contract law and have been transformed into regulatory law. The trading in securities and the execution of orders related to securities in the form of financial services are subject to multiple requirements, such as but not limited to client classification, the duty to stay educated, the duty to inform clients and the duty to document and justify.<sup>83</sup> No suitability and appropriateness test must be made by financial intermediaries who are solely executing or forwarding orders related to securities initiated by clients.<sup>84</sup> An important behavioural conduct rule in the context of the execution of trades in securities is the duty of «best execution». Financial intermediaries must ensure that any execution made for clients is done as optimally as possible in terms of price, time of execution and other

<sup>77</sup> Art. 30 SESTO.

<sup>78</sup> Art. 31 SESTO.

<sup>79</sup> Art. 31 Swiss Financial Market Infrastructure Ordinance (FMIO) (SR 958.11).

<sup>80</sup> Art. 4.3.3. SIX Swiss Exchange Ltd. Rule Book of 15/06/2017.

<sup>81</sup> Art. 3 para. a chiff. 2 and 8, and para. c FinSA.

<sup>82</sup> Art. 3 para. d. chiff. 1 and 2 FinSA.

<sup>83</sup> See Art. 4, 6, 8 and 9 Bundesgesetz über die Finanzdienstleistungen (Finanzdienstleistungsgesetz, FinSA).

<sup>84</sup> Art. 14 para. 1 FinSA.

criteria.<sup>85</sup> Securities lending activities related to securities of clients require specific prior written consent.<sup>86</sup>

#### *Organisational requirements*

Investment firms trading in securities or executing orders related to securities are also subject to organisational requirements addressing conflict of interest situations and inducements.<sup>87</sup> The new regulatory obligations about inducements orient themselves particularly closely towards the case law related to discretionary asset management agreements.

#### *Investment firms trading in securities under the FinIA regime*

Under the new FinIA regime<sup>88</sup> securities dealers will be called investment firms to be in line with the EU terminology.<sup>89</sup> According to FinIA an investment firm is – or is at least supposed to be – regulated identically to a securities dealer under the SESTA. Any professional trading on one's own account or on behalf of clients in securities thus requires a license as an investment firm.<sup>90</sup> The draft-FINIA also states, however, that proprietary traders who are members of a trading venue, but who do not reach an annual turnover of CHF 5 billion, must be licensed as securities dealers. An investment firm can have accounts for the settlement of securities. Securities can also be held with third parties.<sup>91</sup> However, it cannot take deposits from third parties. Any such activity

requires a banking licence.<sup>92</sup> Every investment firm is subject to minimal capital requirements, regulatory capital requirement, liquidity and risk management obligations.<sup>93</sup> It has to record the orders received and the executed transaction and will have to do the required reporting to the regulator.<sup>94</sup>

#### 1.4.4 Regulation of facilities for the trading in bonds

##### *Stock exchange, MTF, and OTF*

Bonds can be traded in Switzerland on three main facilities, namely the stock exchange,<sup>95</sup> multilateral trading facility (MTF),<sup>96</sup> and the organised trading facility (OTF). Stock exchanges and MTF are also called trading venues and differentiate themselves mainly in the listing of securities. Securities that are not listed on a MTF, meaning that there is no admission of a security in accordance with a standardised procedure whereby requirements regarding issuer and securities are being verified.<sup>97</sup> Bonds are currently traded on the SIX Swiss Exchange, the SIX Corporate Bonds (MTF), and BX Berne Exchange.

In Switzerland, an OTF is the default facility for many other trading set-ups encompassing bilateral<sup>98</sup> and multilateral<sup>99</sup> as well as discretionary and non-discretionary trading activities in both securities and financial instruments, meaning any other financial

<sup>85</sup> Art. 20 para. 1 FinSA.

<sup>86</sup> Art. 21 para. 1 FinSA.

<sup>87</sup> Art. 27 and 28 FinSA.

<sup>88</sup> Bundesgesetz über die Finanzinstitute (Finanzinstitutsgesetz, FinIA).

<sup>89</sup> Art. 2 para. 1 lit. e FinIA.

<sup>90</sup> Art. 37 para. 1 lit. a FinIA.

<sup>91</sup> Art. 40 para. 1 lit. b FinIA.

<sup>92</sup> Art. 40 para. 3 FinIA.

<sup>93</sup> Art. 41 to 43 FinIA.

<sup>94</sup> Art. 46 and 47 FinIA.

<sup>95</sup> Art. 26 para. 1 chiff. b Swiss Financial Market Infrastructure Act (FMIA/FinfraG). A stock exchange means an institution for multilateral securities trading

where securities are listed, whose purpose is the simultaneous exchange of bids between several participants and the conclusion of contracts based on non-discretionary rules.

<sup>96</sup> Art. 26 para. 1 chiff. c FMIA. A MTF means an institution for multilateral securities trading whose purpose is the simultaneous exchange of bids between several participants and the conclusion of contracts based on non-discretionary rules without listing securities.

<sup>97</sup> Art. 2 para. 1 chiff. f FMIA.

<sup>98</sup> See FINMA Circular 2018/1 Organised trading facilities chiff. 23, bilateral trading involves always the operator of the facility as counterparty. He also takes market risk.

<sup>99</sup> See Art. 22 para. 1 Swiss Financial Market Infrastructure Ordinance (FMIO/FinfraV).

instruments used for investment purposes not being securities.<sup>100</sup> Trading activities on an OTF is any trading activity that (i) is governed by a set of rules that is standardised and binding to participants, (ii) allows for the conclusion of contracts within the scope of application of these rules, and (iii) takes place when the initiative to trade can come from the participants.<sup>101</sup> An OTF can only be operated by a bank, securities dealer, trading venue, facility recognised as a trading venue, or a legal entity within a financial group that is controlled directly by a financial market infrastructure and is subject to consolidated FINMA supervision.<sup>102</sup> Unlike under MiFID II/MiFIR, a systematic internaliser is, under the Swiss regime, not a special category of investment firm/securities dealer, but is either a bilateral OTF or securities dealer if these requirements are met.

#### *Organisational requirements of trading venues*

The organisational requirements of all trading venues (MTF and Stock Exchange) are identical in their core and subject to their own regulatory and supervisory organisation which is appropriate for their activities and approved by FINMA. Trading venues must ensure an adequate organisation of the trading activities from a regulatory, technical, and organisational point of view that allows for pre- and post-trade transparency of bid and ask prices and related volumes.<sup>103</sup> They have to appoint an independent body responsible for the regulation of the activities of the trading venue and the listing of securities in the case of a stock exchange<sup>104</sup> and the admission of securities in the

case of an MTF.<sup>105</sup> Participants can either be securities dealers, foreign market participants, or other parties supervised by FINMA.<sup>106</sup> The trading and compliance of the participants with the rules and regulations must be supervised by an independent body which has to inform FINMA in case of illicit activities and irregularities.<sup>107</sup> Certain admissions or delistings of securities and participants might be appealed with an independent appellate body.<sup>108</sup> Trading venues must designate trading activities resulting from algorithmic trading activities. Participants engaging in algorithmic trading activities are also subject to specific requirements applicable to their systems.<sup>109</sup>

#### *Organisational requirements of an OTF*

The operation of an OTF is also subject to requirements that ensure an orderly trading, transparency, and investor protection, such as best execution requirements in case of discretionary trading.<sup>110</sup> Any operator of an OTF must issue rules and regulations and appoint an independent control function that monitors compliance with these regulations.<sup>111</sup> Pre-trade transparency is required in the case of bilateral and multilateral liquid trading, meaning at least 100 trades on average per day over the last year.<sup>112</sup> Post-trade transparency is only required in the case of multilateral trading.<sup>113</sup> Anyone operating an OTF or intending to do so in the future must report this fact to FINMA.<sup>114</sup>

<sup>100</sup> See Art. 3 lit. b Draft-Swiss Financial Services Act (FinSA/FidleG)

<sup>101</sup> FINMA Circular 2018/1 Organised trading facilities chiff. 5.

<sup>102</sup> Art. 43 FMIA.

<sup>103</sup> Art. 27 and 29 FMIA. See also Art. 27 and 28 FMIO.

<sup>104</sup> Art. 35 FMIA.

<sup>105</sup> Art. 36 FMIA and Art. 24 Swiss Financial Market Infrastructure Ordinance (FMIO).

<sup>106</sup> Art. 34 FMIA.

<sup>107</sup> Art. 31 FMIA.

<sup>108</sup> Art. 37 FMIA.

<sup>109</sup> Art. 31 FMIO.

<sup>110</sup> Art. 39 FMIO.

<sup>111</sup> FINMA Circular 2018/1 Organised trading facilities chiff. 30 et seq.

<sup>112</sup> Art. 42 FMIO. FINMA Circular 2018/1 Organised trading facilities chiff. 37 et seq.

<sup>113</sup> Art. 43 FMIO.

<sup>114</sup> FINMA Circular 2018/1 Organised trading facilities chiff. 42.

### *Trading in bonds under MiFID II/MiFIR*

Under the MiFID II/MiFIR-regime, bonds can be traded on regulated markets, multilateral trading facilities, organised trading facilities, and through systematic internalisers if dealing is done on one's own account, when executing client orders outside a regulated market,<sup>115</sup> MTF,<sup>116</sup> or OTF<sup>117</sup> on an organised, frequent systematic and substantial basis.<sup>118</sup>

#### 1.4.5 Regulation of Swiss investment firms trading securities in the EU markets

##### *Trading in securities as an investment service under MiFID*

Dealing on one's own account, the execution of orders on behalf of clients, and the reception and transmission of orders in relation to one or more financial instrument, such as transferable securities in the form of bonds, is an investment service under MIFD I and MiFID II.<sup>119</sup>

##### *Provision of investment services to clients domiciled in the EU on a pure cross-border basis*

Swiss-domiciled investment firms providing investment services to clients domiciled in the EU on a pure cross-border basis are so-called «third country investment firms»<sup>120</sup> and are able to continue to provide services and activities in EU member states in accordance with the national regimes until three years after the adoption of the equivalence decision of the European Commission according to Art. 47 MiFIR.<sup>121</sup> The principle of «reverse solicitation» allowing for the unrestricted

provision of an investment service to EU-domiciled clients will, however, remain applicable to a situation in which a client domiciled in the EU initiates such services at its own exclusive initiative.<sup>122</sup> EU member states could, at least theoretically, also require that a Swiss-based investment firm trading in bonds on a pure cross-border basis would have to establish a branch in this territory.<sup>123</sup>

##### *Membership of an EU-based trading venue*

The pure fact that a Swiss-domiciled investment firm is trading on an EU-based regulated market on a pure cross-border basis without having clients domiciled in the EU is not an investment service in the sense of MiFID II. It is thus under the discretion of the individual member states to impose restrictions and obligations on such trading activity. Member states typically require a regulation by means of remote access or by setting up a branch in the host member state.<sup>124</sup>

#### 1.4.6 Regulation under Swiss anti-money laundering regulations

##### *Application to securities dealers*

Securities dealers duly licensed by FINMA are financial intermediaries according to Art. 2 para. 2 lit. b AMLA.<sup>125</sup> They are subject to the requirements of the Swiss anti-money laundering provisions. Any other trading activities are not subject to the Swiss anti-money laundering regulations.<sup>126</sup> By analogy, entities trading in financial instruments that are not securities do not

<sup>115</sup> See definition in Art. 4 para. 1 chiff. 21 MiFID II.

<sup>116</sup> See definition in Art. 4 para. 1 chiff. 22 MiFID II.

<sup>117</sup> See definition in Art. 4 para. 1 chiff. 23 MiFID II.

<sup>118</sup> See Art. 13 Commission Delegated Regulation (EU) 2017/565 of 25 April 2016.

<sup>119</sup> Annex I Section A chiff. 1, 2, 3, and Section C chiff. 1 Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2001/92/EC and Directive 2011/61/EU (MiFID II).

<sup>120</sup> Art. 4 para. 1 chiff. 57 MiFID II.

<sup>121</sup> Art. 54 para. 1 Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (MiFIR).

<sup>122</sup> Art. 46 para. 5 MiFIR and Art. 42 MiFID II.

<sup>123</sup> Art. 39 para. 1 MiFID II.

<sup>124</sup> See Art. 36 MiFID II.

<sup>125</sup> Federal Act on Combating Money Laundering and Terrorist Financing (SR 955.0).

<sup>126</sup> Art. 5 para. 2 Federal Ordinance on Combating Money Laundering and Terrorist Financing (AMLO) (SR 955.01).

fall within the scope of application of Swiss anti-money laundering regulations. The key requirements securities dealers have to fulfil are the verification of the identity of contractual parties and the establishment of the identity of the controlling person and the beneficial owner according to the CDB16.<sup>127,128</sup>

#### *Identification of the client*

The securities dealer must verify the identity of the contracting partner when establishing business relationships. The execution of transactions involving trading in securities must exceed CHF 25,000 in case of an account opening.<sup>129</sup> For natural persons, the following topics must be appropriately documented:<sup>130</sup>

- Name,
- First name,
- Date of birth,
- Nationality and the actual domicile address, as well as
- Means used to prove identity.

For legal entities and partnerships, the following topics must be appropriately documented:

- Company name,
- Actual registered office, as well as
- Means used to prove identity.

#### *Establishment of the identity of controlling persons and beneficial owners*

If an operating legal entity or partnership has one or more controlling persons with voting rights or capital shares of 25 percent or more, these are to be identified in writing. Controlling persons are

those natural persons who effectively have ultimate control over the company. Whether these persons exercise control directly or indirectly via intermediate companies is irrelevant. A controlling person must generally be a natural person. The contracting partner must confirm the name, first names and actual domicile address of the controlling person in writing or by using Form K.<sup>131</sup>

The bank requires, from its contracting partner, a statement concerning the beneficial ownership of the assets. Generally, the beneficial owners of the assets are natural persons.<sup>132</sup> If the contracting partner declares that the beneficial owner is a third party, then the contracting partner has to document the latter's last name, first name, date of birth and nationality, along with actual domicile address, or the company name, address of registered office and country of registered office using Form A.<sup>133</sup>

#### *Business relationships and transactions with increased risk*

Securities dealers have to determine business relationships and transactions that are subject to increased risk.<sup>134</sup> The initiation of such business relationships and the execution of such transactions are subject to enhanced due diligence requirements.<sup>135</sup> Such business relationships must be approved by the management.<sup>136</sup>

#### *Organisation*

The securities dealer must establish an organisation that allows for efficient compliance with the applicable anti-money laundering regulations and, in particular, must designate a dedicated anti-money laundering function.<sup>137</sup> New

<sup>127</sup> Agreement on the Swiss Banks' Code of Conduct with regard to the exercise of due diligence (CDB16).

<sup>128</sup> Art. 35 Federal Ordinance on Combating Money Laundering and Terrorist Financing of FINMA (AMLO-FINMA) (SR 955.033.0).

<sup>129</sup> Art. 4 para. 1 and 2 CDB.

<sup>130</sup> Art. 7 CDB.

<sup>131</sup> Art. 21 CDB.

<sup>132</sup> Art. 27 para. 1 CDB.

<sup>133</sup> Art. 28 para. 1 CDB.

<sup>134</sup> Art. 13 and 14 AMLO-FINMA.

<sup>135</sup> Art. 15 AMLO-FINMA.

<sup>136</sup> Art. 19 AMLO-FINMA.

<sup>137</sup> Art. 24 AMLO-FINMA.

products must be checked by the securities dealer for their compliance with the applicable regulations. Securities dealers must, in particular, establish an effective mechanism for the surveillance of the transactions and the business relationships based on an IT system.<sup>138</sup>

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<sup>138</sup> Art. 20 AMLO-FINMA.





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