



## **“SFBC report on sanctions”**

Report of the Swiss Federal Banking Commission on the applicable sanctions with respect to its supervision of the banks, securities traders and fund management companies (“institutional supervision”) and to its role as market regulator with regard to insider trading, share price manipulation and other violations of market behaviour rules (“market supervision”) with a view to the restructuring of the financial market supervisory function in Switzerland.

*English translation of the report’s foreword and summary. The full report is available in French and German.*

**April 2003**



## Foreword

Over the past few years, the Swiss Federal Banking Commission has, on various occasions, publicly pointed to the lack of effective and consistent sanctions in the area of supervisory law. There are shortcomings not only in the supervision of banks, securities traders, fund management companies and auditors (institutional supervision) but also of the stock exchanges (market supervision). In this report, the Swiss Federal Banking Commission presents concrete proposals on how to remedy these shortcomings.

The SFBC approved the initial version of the November 2002 sanction report and the accompanying legislative proposals at its meeting of 25 November 2002 and, in December 2002, passed them on to the expert commission on financial market regulation appointed by the Swiss Federal Council and headed by Professor Ulrich Zimmerli. Zimmerli's expert commission has decided to address the issue of sanctioning instruments of the planned new financial market regulator ("FINMA") in the second half of 2003. Simultaneously, the report was also circulated to the working group headed by Mr. Hanspeter Uster, member of the council of the canton Zug, for comments. This working group has been commissioned by the heads of cantonal justice and police departments to review the provisions on stock market infractions (components of such infractions and related penal procedure).

The Swiss Federal Banking Commission, with this report, seeks to contribute to the discussion on the introduction of effective sanctioning instruments corresponding to the needs of a modern financial market regulatory authority. In this context, it has approved an extended version of the report at its meeting of 24 April 2003 which will be published at the occasion of the annual press conference of the Swiss Federal Banking Commission in April 2003.

Dr. Kurt Hauri  
Chairman of the Swiss Federal Banking Commission

April 2003



## 1. Overview

*The sanctioning instruments which the SFBC currently has at its disposal for institutional and market supervision are insufficient. This point has been raised not only by the SFBC but also by other national and international bodies.*

*Supervision of approved banks and securities traders (institutional supervision) as it is practised today knows no sanctions other than licence revocation, removal of individuals in positions of authority (individuals required by law to present the guaranties of an irreproachable activity), and the issuance of an official reprimand. Therefore, serious cases for which licence revocation would be too severe and the removal of individuals in positions of authority inappropriate due to the lack of direct responsibility, go unpunished as there are currently no means to impose disgorgements of illegal gains or fines.*

*In the area of market regulation, i.e. the supervision of standards in securities trading with the aim of detecting or preventing insider dealing or share price manipulations, the current situation is equally unsatisfactory. This circumstance results from the sharing of competences between the cantonal penal authorities and the SFBC. For instance, the prohibitions under criminal law on the misuse of insider information and on share price manipulation apply to everyone. However, when supervising the approved institutes and their employees, the SFBC sets stricter standards. This leads to discrimination insofar as supervised and unsupervised market participants are treated differently. In addition, the penal standards currently in force are too narrowly defined: for example, the exploitation of the confidential knowledge that the profits of a particular company will be below forecasts and below the expectations of other market participants, is not a criminal offence. In such cases, only licensed institutions and their employees can be sanctioned.*

*To address these issues, the report proposes to include an array of administrative sanctions in the law on financial market regulation ("FINMAG"), which is currently being drafted, and which the future financial market regulator ("FINMA") would then be able to impose:*

- *FINMA should be given the power to impose both financial sanctions and suspension of professional activity by way of administrative ruling.*
- *In the case of institutional supervision, serious breaches of the conditions of the licence and, in the case of market supervision, market abuse offences, should be recognized as infractions pursuant to a new definition to be added to the Stock Exchange Act and carried through by FINMA.*
- *Sanctions should be applicable both against natural persons and legal entities; the latter could avoid sanctions by showing that every organisational measures necessary to prevent abuse have been taken. On the other hand, preventive supervisory procedures against individuals should be abandoned in favor of sanctioning procedures.*
- *The procedure should be essentially aligned with the Administrative Procedure Act, but expanded and reinforced by elements of Federal Penal Procedure Act rather than Federal Civil Procedure Act as is currently the case.*



- *According to the proposal, an independent sanction committee should be created within FINMA, which would make decisions following a special sanctioning procedure and would meet the requirements of the European Convention on Human Rights with regard to penal procedures.*
- *Legal recourse against decisions by FINMA should be available under the standard federal law procedures (appeal to the Federal Supreme Court or – after the entry into force of the justice reforms – Federal Administrative Court with option to appeal further to the Federal Supreme Court).*
- *The penal infractions punishable under administrative law that are included in the current versions of the laws on supervision should be reduced to a minimum and the remaining offences should relate to procedures for administrative sanctions.*
- *Insider trading and share price manipulation should, according to the proposal, remain in the Swiss Penal Code. They should only be a matter for the penal authorities local to the stock exchange in very serious cases and at the request of FINMA. All other cases should be dealt with by FINMA using administrative sanctions.*
- *The higher level of supervision exercised by FINMA over the self-regulating activity of the stock exchange should be enhanced. FINMA should be able to issue relevant regulations in those areas where the stock exchange failed to do so following the request of FINMA or only partially did so.*
- *The sanctioning system of the stock exchange for breaches of self-regulation (for example in the case of issuers failing to meet ad hoc advertising requirements) should be enhanced in terms of supervisory law. In serious cases, FINMA should be able to take over a disciplinary procedure from the stock exchange and to pursue it under administrative sanctioning procedure.*

*In the SFBC's opinion, these proposals seek to enable FINMA to impose adapted sanctions both in the case of institutional as well as market supervision. It would allow a more flexible approach to dealing with offences that relate to market abuse outside the constraints of criminal law. This model will substantially simplify procedures and, if endowed with sufficient resources, would shorten the time required to implement sanctions, especially as far as market supervision is concerned. The proposals also eliminate administrative law offences, which have largely fallen in desuetude, replacing them with administrative sanctions where necessary. Those affected would benefit from the same procedural guarantees as afforded by penal procedures. Decisions in the first instance would be made by a specialist sanction committee, appointed by the Federal Council and independent of the management of the supervisory authority, thus making the sanctioning procedure more transparent for the market and the general public and thereby increasing the credibility and the effectiveness of the regulator.*

*As far as market supervision is concerned, the essential point is that, with this model, market behaviour rules be enforced equally for all market participants, irrespective of whether their employer is a company supervised by FINMA or not. Moreover, this model is the only one allowing an harmonized regime of supervision and sanctioning applicable to the markets, the institutions and the private investors. In the SFBC's opinion, the*



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*proposal to address market abuses in the context of supervisory legislation instead of penal law will not damage the credibility of the rules. On the contrary, since this shift would be accompanied by faster procedures and the development of a unified jurisprudence established by a specialist authority that will offer transparency for the general public.*

*In December 2002, the SFBC sent an initial version of this report to the Zimmerli expert commission appointed in December 2001. The latter was commissioned by the Federal Council on 30 November 2001 not only to examine the creation of an integrated financial market regulator and to report to the Federal Council but also to look into ways to improve the sanctioning powers of this new regulator.*