No breach of art. 56 of the Listing Rules regarding Disclosure of Management Transactions

Decision

1. X Ltd did not breach Article 56 LR in conjunction with Article 2 DMT.
2. A short summary of this decision and its reasons will be published by SIX once it is in force.
3. X Ltd shall bear the costs of the procedure amounting to CHF […].
4. [instruction on the right to appeal]

Reasons for the decision

1. The Sanction Commission received a proposal from SIX Exchange Regulation ("SER") to issue a reprimand against X Ltd ("X Ltd") for a repeated breach of the obligation of Article 2 (2) of the Directive on Disclosure of Management Transactions (DMT) in not having taken action against individuals non-compliant with the DMT.
2. X Ltd did not challenge the facts set out by SER but considered not having breached any of its obligations under the applicable regulations.

A. The facts

3. On [date], X Ltd disclosed seven transactions involving the acquisition of [quantity] registered shares with an aggregate value of CHF […]. The transactions had been carried out by [person Y], a member of X Ltd's Board of Directors, between [date], up to one and a half months before they were reported to SER.
4. X Ltd explained in a letter to SER by its lawyer also dated [date] the reasons for this late disclosure in that [person Y] instructed her/his staff to report the transactions to X Ltd, which they subsequently failed to do. [Person Y] further assumed that her/his staff would disclose the transactions to X Ltd within the prescribed time limit, as allegedly instructed. In a reply to this letter dated [date], SER reminded X Ltd that the person subject to the reporting obligation continues to be responsible for disclosing management transactions, even if the duty had been delegated to third parties. Moreover, SER reminded X Ltd of its obligation to ensure that persons subject to the reporting obligation comply with their obligations and, if necessary, to take action against any individuals who fail to discharge their obligations within the time limit set in Article 2 (2) DMT. SER in this letter also warned X Ltd that an investigation may be initiated upon any recurrence of such breach, potentially leading to the imposition of a sanction.
5. Later in the same year, on [date], lawyers acting on behalf of X Ltd notified SER that X Ltd intended, that same day, to publish some transactions, which had been carried out long before, i.e. during the previous year by a member of its Group Executive Committee, [person Z], but not reported according to the rules of DMT. The lawyers explained the reasons for the delay in reporting: [Person Z] had presumed that the bank person Z had instructed to execute the transactions would report the transactions to X Ltd. Person Z assumed that the bank in charge of executing the transactions would disclose the information required directly to X Ltd, as transactions had always been reported directly to X Ltd by the bank in charge of administering the stock option plan for the person required to report the transactions. But [person Z] used a different bank and

did not verify that this bank was also bound to disclose the relevant transactions to X Ltd.

6. On the same [date], X Ltd disclosed, via the electronic reporting and publication platform, four management transactions which had been carried out by [person Z] on [date], [date], [date] and [date], totaling [quantity] registered shares with a combined value of CHF […].

7. In a letter dated [date], SER asked X Ltd to answer some questions until [date], as part of a preliminary investigation. X Ltd did so timely. On [date], the Audit Committee of X Ltd issued a warning against [person Z] and [person Y]. On [date], SER opened a formal investigation against X Ltd and, on [date], informed the public of the initiation of this investigation. On [date], the case was submitted to the Sanction Commission.

B. <u>The applicable rules</u>

8. Between the time the transactions in question were carried out and today, the obligations in question (Article 56 (2) of the Listing Rules (LR) and Article 2 (2) of the Directive of Management Transactions (DMT) have been formally changed but not materially (in its content). The obligation according to Article 56 (2) LR was stipulated in Article 56 (1) of the previous versions of the LR and the obligation according to Article 2 (2) DMT was stipulated in Article 3 (2) of the previous version of the DMT. Against this background and in view of the readability of the present decision, reference is made to the version of LR and DMT entered in force on April 1, 2011.

9. Article 56 (2) of the LR provides that issuers must ensure that members of their board of directors and of their executive committee report transactions in the issuer's shares, or in related financial instruments, to the issuer no later than the second trading day after the reportable transaction has been concluded. The issuer must instruct and train the persons subject to the reporting obligation appropriately and effectively and regularly remind them about the obligation to disclose management transactions (n 11 of Commentary re Art. 56 LR and the Directive of Management Transactions - Commentary MT).

10. It is undisputed in the present case that X Ltd has been properly organized according to DMT. X Ltd has presented credible evidence that members of its Group Executive Committee and Board of Directors received adequate training and regular reminders of their duty to disclose management transactions, as required by the rules. X Ltd has also adopted internal guidelines (… Policy), explaining in detail the obligation to disclose management transactions, which have been issued to the relevant individuals.

11. SER did not apply for a reprimand because of a lack of organization, but because X Ltd did not take action against [person Z] though there was recurrence as mentioned in n 82 Commentary MT.

12. It is obvious that the Exchange may impose sanctions to issuers only, but not to the persons failing in their reporting obligations. The latter is in the responsibility of the issuer. The Sanction commission had to first clarify whether there was "recurrence" and secondly whether X Ltd has violated its obligation to take action against a person who failed to comply with the reporting obligations.

<u>Recurrence</u>

13. In [month] [year], - as mentioned - a member of the Board, [person Y], did not report seven transactions. X Ltd did realize this in [month] [year] and immediately reported it to SER. Then in [month] the same year, X Ltd noted that another person, namely a member of its Executive Committee, [person Z], did not report four transactions that had

been executed in the course of the previous year […]. SER stated that a recurrence of a breach according to Commentary MT, note 82, is deemed to exist where there has been a repeated breach of reporting obligations by the same or different individuals. A recurrence is deemed to have occurred whether the disclosure obligations were breached on repeated occasions by the same person, or the breaches were committed by different individuals.

14. The wording of Art. 2 (2) DMT reads as follow: „The issuer is responsible for holding the persons subject to reporting obligations to their reporting obligation and, as the case may be, for taking appropriate action against them."[i] The comment to this article reads (Commentary MT, note 82): "If a person subject to the reporting obligation breaches his/her reporting obligation, the issuer must take action against the person subject to the reporting obligation, at least in cases of recurrence."[ii] This formulation cannot be understood otherwise than that an action is meant against a one and only specific person within the company. This is also apparent from the context of the immediately preceding note concerning the suspicion on one (not several) person: „If an issuer suspects that a person subject to the reporting obligation failed to fulfil the reporting obligation in a specific instance[iii], it must contact this person and take appropriate action to hold the person to his/her reporting obligation."

15. If the Exchange would define a recurrence also as a case in which a person fails to report after another person in the same company had already failed to report, the note in the Commentary MT would need to be formulated differently. The present formulation states that for first violators, the issuer might refrain from sanctioning if an action seems not be appropriate. It is in its discretion to take action against first violators. The mandatory obligation of an issuer to sanction a person exists only if the same has repeatedly breached the reporting obligation.

16. In the present case where first in [year] a member of the Executive Committee failed to report correctly and later in the following year another person, member of the Board of directors, failed as well, there is no recurrence in the sense of note 82 Commentary MT.

<u>Action against non-compliant individuals</u>

17. SER stated that, in essence, X Ltd ought to have taken action against [person Y] and [person Z] once it became aware of the non-compliance with the reporting deadlines. "As a minimum, X Ltd ought to have taken action against [person Z] on becoming aware of the breaches committed by person Z..." SER raised that in its letter dated [date], it already explicitly advised X Ltd of its duty to take action in relation to the late notification of transactions by [person Y]. In this letter, however, SER has made general statements only: „X Ltd is reminded that according to Art. 56 aLR the issuer must ensure that the members of the board of directors and senior management report their transactions in accordance with the applicable regulations (…) Repeated breaches of provisions by persons subject to the reporting requirement may lead to a formal investigation and the imposition of sanctions." This wording cannot be understood that SER specifically advised X Ltd to take action against [person Y], as it mentioned the applicable rules only.

18. Issuers (as long as they are properly organized to comply with the obligations of the DMT) are allowed a certain degree of discretion. Article 2 (2) DMT stipulates that the issuer is responsible for holding the persons subject to reporting obligations to their reporting obligation and, as the case may be, for taking appropriate action against them. Only in case of recurrence it is mandatory to take action against a person. Should the issuer be obliged to sanction every first-time offender, the words "at least in cases of recurrence" would be meaningless. X Ltd considered the distribution of the letter of SER of [date], to all members of the Board of directors and of the Executive Committee as an

appropriate action to address the reporting obligations since no other breaches happened before. Because the issuer is granted certain discretion in the cases of first violators, it was not mandatory for X Ltd to sanction the member of its Board that is accused of a violation of her/his reporting obligations for the first time ([person Y], when [person Y] noticed that the seven transactions in [month] were not properly conveyed to X Ltd, informed X Ltd on [date] and X Ltd informed SER on its own initiative on [date]). The handover, in [month] [year], of the letter of SER quoting the applicable regulations may be regarded as a sufficient measure.

19. SER did not open an investigation in [month] [year] when X Ltd announced the improper reporting of the transactions of [person Y] in [month]. It is at least doubtful to reconsider these facts later in accusing X Ltd for not having taken an action against person Y. On the one hand, SER justified its proposal for a reprimand by stating that "X Ltd ought to have taken action against [person Y] and [person Z]". On the other hand, SER stated that X Ltd "should, as a minimum, have taken action against [person Z]." Considering this unclear reasoning, it is assumed that SER did not allege to include [person Y].

20. The omission of the transaction reports of by [person Z] is not a case of recurrence. Person Z was a first time violator. Despite this, the Audit Committee of X Ltd issued a formal warning against [person Z] (and against [person Y]). As mentioned before, an issuer is allowed (but not obliged) to take action against an individual even in a case of a first violation already.

21. SER stated that it must be assumed X Ltd was only prompted to take action against the non-compliant individuals because of the proceedings instituted against it. SER stated that issuing a retrospective warning to [person Y] and [person Z], when under pressure from the proceedings initiated against it, does not have the effect of remedying the breach of DMT.

22. It is conceivable that an issuer that does not proceed to take action on its own, but only because of an investigation by SER, violates Article 2 (2) DMT. But in each case, the time aspect has to be considered.

23. On [date], during the preliminary investigation, SER submitted to X Ltd several questions about the non timely reported transactions by [person Z]. It was asked whether an action was taken against person Z, and if not, why not. SER set a time limit to answer to [date]. X Ltd was not questioned whether it took action against [person Y].

24. Within the time limit of [date], X Ltd on the one hand answered that it distributed the letter of SER of [date], to the persons subject to reporting obligations once it knew of the breach of the reporting obligation by [person Y] (as mentioned before). X Ltd raised that the distribution of this letter had enough impact and it was not necessary to do more. On the other hand in the same answer, X Ltd informed SER that its Board of directors would review the matter on the meeting of [date]. This meeting date had been scheduled long before, but took place after the expiry of the time limit set by SER. So within the limit set by SER X Ltd could neither give information of the result of this review nor of a decision of its Audit Committee that is responsible within X Ltd to take action against persons not compliant with reporting of management transactions (see below).

25. Based on the answers received on [month] [year], SER assumed that X Ltd was only prompted to take action against the non-compliant individuals because of the proceedings instituted against it and that X Ltd should have taken action against [person Z] upon becoming aware of the late reporting by her/him on [date]. According to X Ltd 's internal organization, the Audit Committee is responsible to oversee the compliance of the management reporting obligations and to take actions against non-compliant persons. X Ltd rightly stated that it would be unreasonable to require X Ltd's Audit Committee to hold a special meeting just to analyze the matter of this late reporting. Its previous meeting took place on [date] (i.e. before X Ltd was aware of the breach on

[date]) and the next meeting was scheduled for [date]. On this very first meeting after the late disclosure became known to X Ltd on [date], i.e. within four weeks, the Audit Committee took an action against the non-compliant person. This approach is permissible. It was correct to inform SER immediately. But there was no need to immediately schedule a special meeting for sanctioning. It is to be noted that on [month] [year], X Ltd did take action against the non-compliant persons irrespectively of the then not known result of the preliminary and formal investigation by SER.

26. In summary, X Ltd cannot be accused of having taken an action too late. Furthermore, there is no evidence that only the letter of SER of [date] prompted X Ltd to put the matter on the agenda of its Audit Committee. It is not objectionable – and SER rightfully did not allege this – that in the present case a warning was considered to be adequate by X Ltd. Indeed, formal warnings against members of a Board of Directors or of an Executive Committee of listed companies are deemed to have a negative impact on the reputation of these persons.

27. The present case shows that even with a good organization of the reporting system, where the issuer cannot be criticized, errors may occur. The only way to prevent such errors in an even more efficient way would be the introduction of a mandatory trading venue for the persons subject to reporting obligations, be it via the company's treasury department or through a single designated fiduciary, in automatic contact to the share register. The introduction of such a system would also reduce the need of investigation. It would be appropriate to consider its introduction in the DMT.

C. <u>To the costs and the publication</u>

28. Section 4.5 of the Rules of procedure states that the Sanction Commission may impose charges to cover its procedural expenses. According to section 9.8. of the List of charges of the Listing Rules, the related charges of sanction proceedings shall be determined according to expenditures involved. In the present case, the costs of SER amounted to CHF […], the cost of the Commission to CHF […]. The total of CHF […] is imposed to X Ltd. X Ltd is expressly advised of the recommendation in note 83 of Commentary MT.: "The issuer is invited to impose to the persons failing to comply with the reporting obligations 'sanctions such as, for example, payment of the costs of possible sanction procedures (...)'".

29. The opening of the investigation against X Ltd was published by SER. Consequently, the result of a previously announced investigation has also to be published. This is also consistent with section 6.3 para. 1 of the Rules of procedure stating that the Commission has to publish sanction decisions that come into legal force. That applies in the present case. The publication will summarily point out that X Ltd did not breach its obligations under the DMT and that the warnings issued by it were permissible.

30. Furthermore and as prescribed in section 6.3 para. 3 of the Rules of procedure, the full text of the legally enforceable decisions in a completely anonymised version are available on the SIX Exchange Regulation Website.

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[i] German version: „Der Emittent hat die meldepflichtigen Personen zur Meldung anzuhalten und gegebenenfalls gegen diese vorzugehen."

[ii] German version: „Ist eine Verletzung der Meldepflichten *einer* meldepflichtigen Person zuzurechnen, hat der Emittent, zumindest im Wiederholungsfall, gegen *die* meldepflichtige Person vorzugehen."

[iii] The translation of the German version "im konkreten Fall" should be read "in a specific case".