Decision

in the procedure SaKo 2020 SaKo-RLE-II/19

SIX Exchange Regulation (SER)
Hardturmstrasse 201
8005 Zurich

vs.

X. ___ (X. ___)
[address]
[place]

The **Sanctions Commission** - […], Chairman, […], […], […], secretary - has rendered a decision as follows, following the sanction proposal submitted by SIX Exchange Regulations:

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1. X. ___ violated the applicable financial reporting standard Swiss GAAP FER (Swiss GAAP FER 20, Swiss GAAP FER 30, and Swiss GAAP FER Framework) in a grossly negligent manner and thereby its obligations pursuant to Art. 51 LR in combination with Art. 6 DFR:
    a. by not accounting for a material impairment on its investment in [Investment Entity] in the [20X1] Swiss GAAP FER annual financial statements;
    b. by erroneously consolidating [Investment Entity] as a subsidiary starting [first day of the reporting period] [20X2] in the [20X2] Swiss GAAP FER interim financial statements; and
    c. by materially misstating both the [20X1] Swiss GAAP FER audited annual and [20X2] Swiss GAAP FER unaudited interim financial statements that consequently did not give a true and fair view of X. ___'s financial situation and were thus unreliable.
2. X. ___ pay a fine of CHF 40,000 (Art. 61 para. 1, number 2 LR).
3. X. ___ shall bear the cost of SER for the enforcement procedure in the amount of CHF […] and the costs incurred by the Sanctions Commission in the amount of CHF […] (Ciph. 3.7 LocRB), corresponding to a total amount of costs of CHF […].

The legally binding decision of the Sanctions Commission will be published on SIX Exchange Regulation AG's website in anonymous form (Ciph. 6 para 8 RP).

[…]

Reasons for the decision

1. On [date] [20X1], X. ___ (**X. ___**, **Company** or **Issuer**) acquired an investment […] in [Investment Entity], a [place], [county], corporation, (**the Investment**) for a consideration of [currency] [amount]. As of [reporting period-end] [20X1], X. ___ performed an impairment test for the Investment in [Investment Entity] that contained mechanical errors, implausibly aggressive assumptions, and lacked due care in the process of its preparation. SER finds, and the SaKo concurs, that as a result, the Investment has been materially overstated in the balance sheet and a material impairment expense was missing in the income statement of the [20X1] Swiss GAAP FER (**FER**) annual financial statements. X. ___ restated in its [20X2] FER annual financial statements the carrying amount of [Investment Entity] from [currency] [amount] to [currency] [amount] and retrospectively recorded a material impairment of [currency] [amount] in the income statement for the financial year [20X1].
2. X. ___ consolidated the Investment as of [first day of the reporting period] [20X2] even though X. ___ did not possess control over [Investment Entity] in the first half-year of [20X2]. As a consequence, the [20X2] FER interim financial statements were materially misstated in the view of SER, and to which the SaKo concurs, X. ___ corrected this erroneous consolidation of [Investment Entity] starting [first day of the reporting period] [20X2] in both its [20X2] FER annual financial statements and its [20X3] FER interim financial statements.

1. Procedure

1.1. Overview of proceedings

3. In accordance with Art. 51 Listing Rules (**LR**[1]) in conjunction with Art. 6 of the Directive on Financial Reporting (**DFR**[2]), SIX Exchange Regulation AG's (**SER**) review is aimed at monitoring compliance of the issuers' financial statements with the applicable accounting standards.
4. The accounting standards applicable to X. ___'s [20X1] annual financial statements authorized for issue and published on [date] [20X2], to X. ___'s [20X2] interim financial statements authorized for issue on [date] [20X2] and published on [date] [20X2] and to X. ___'s [20X3] interim financial statements authorized for issue on [date] [20X3], initially published on [date] [20X3] as well as republished as a corrigendum on [date] [20X3] are FER.
5. After reviewing the [20X1] FER annual financial statements of X. ___, SER initiated a preliminary investigation on [date] [20X2], requesting clarification on various topics. X. ___ timely filed its statement to the preliminary investigation on [date] [20X2] and a reply to additional questions by SER on [date] [20X2] and to further questions on [date] [20X2].
6. After having considered all the evidence, SER concluded that there were indications of a potential violation of the obligations set out by the applicable accounting standard (FER) in connection with X. ___'s [20X1] FER annual and [20X2] FER interim financial statements. Therefore, on [date] [20X3], SER opened an investigation. X. ___ submitted its response statement dated [date] [20X3].
7. SER submitted the sanction proposal for comment to X. ___ on [date] [20X4]. X. ___ submitted its response on [date] [20X4], stating that X. ___ agrees with the facts and findings and that X. ___ does not oppose the legal analysis by SER but refrains from commenting on it. However, X. ___ requests that the sanction shall be lowered taking into account the Company's current financial situation.

[1] Listing Rules (LR) dated 4 November 2016, entry into force 1 May 2017, and LR dated 4 April 2018, entry into force 25 May 2018

[2] Directive on Financial Reporting (DFR) dated 15 September 2016, entry into force 1 May 2017, and DFR dated 20 March 2018, entry into force 1 May 2018

8. Upon request of the Sanctions Commission, X. ___ provided, on [date] [20X4], as additional information the Company's Annual Report [20X3], "all relevant press releases in [20X4]" and the last notification from the [place] Court concerning the suspended bankruptcy procedure, dated [date] [20X4].

1.2. Applicable rules and jurisdiction

9. X. ___ is a company incorporated under [country] law with its registered office in [place]. The Company's [securities] are listed in the "[regulatory segment]" of SIX Swiss Exchange Ltd. X. ___ signed a declaration of approval on [date] [20X3], accepting to be bound by the stock exchange's regulations, especially by the LR and the Rules of Procedure (**RP**[3]) in their most recent version (and on [date], A. ___ Inc., the former name of the Company prior to the change to the current name).

10. The violation of the LR, any additional regulations thereto, or any implementation decrees thereof, may be sanctioned by one or more of the sanctions listed in Art. 61 LR (Art. 60 LR).

11. Competent to decide upon sanction proposals submitted by SER is the Sanctions Commission (SaKo) (Ciph. 3.4 and Ciph. 4 RP). According to Ciph. 6 para. 7 RP, the public will be informed of the investigation concluded by a legally binding sanction decision. In addition, the legally binding decision of the Sanctions Commission will be published on SER's website in anonymous form (Ciph. 6 para. 8 RP).

12. In accordance with Ciph. 6 para. 2 RP, SER has informed the public that an investigation had been initiated, upon dispatch of the sanction proposal to the Sanctions Commission.

2. Facts

2.1. General Comments

13. Art. 49 and Art. 50 LR require issuers to publish annual and interim reports, comprising financial statements in accordance with the applicable financial reporting standard recognized by the regulatory board (Art. 51 LR). The financial reporting standard chosen by X. ___ and applicable to its annual and interim financial statements is FER. FER is a financial reporting standard recognized by the Regulatory Board (Art. 6 DFR).

14. SER has excluded the [20X1] FER interim financial statements of A. ___ Inc. from the current investigation. Therefore, the [20X1] FER interim financial statements of A. ___ Inc., including any possible errors therein, do not form part of this sanction proposal.

15. Furthermore, SER decided not to pursue any other possible errors pertaining to the [20X2] FER annual and [20X3] FER interim financial statements of X. ___ and unrelated to those proposed for sanctioning in the present sanction proposal. In order not to unduly delay the sanction proceedings, SER decided to to limit its sanction proposal to documented, verified, and, in the meantime, corrected errors in the [20X1] FER annual and [20X2] FER interim financial statements. SER considered in the proposal only those parts of X. ___'s [20X2] FER annual and [20X3] FER interim financial statements that include the correction of the errors made in the [20X1] FER annual and [20X2] FER interim financial statements and disregarded for this sanction proposal the remaining parts of the financial statements. However, SER reserves the right to open separate proceedings on the [20X2] FER annual and [20X3] FER interim financial statements or any other future financial statements of X. ___.

2.2. Description of the Case

16. On [date] [20X1], X. ___ acquired the Investment for a consideration of [currency] [amount]. The purchase agreement included three options:

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[3] Rules of Procedure (RP) dated 8 November 2019, entry into force 1 April 2020.

1) A short-dated-break-option giving the seller the right to revoke the agreement before [end of first month of the reporting period] [20X2] by paying [currency] [amount] in cash;

2) An option for the seller to repurchase the stake in [Investment Entity] for [amount] in cash, valid until [end of the fifth month of the reporting period] [20X2];

3) An option for X. ___ to acquire an additional […]% interest in [Investment Entity], including full transfer of control of the board of directors and management, for a price of [currency] [amount].

In the consolidated balance sheet as per [annual reporting period-end] [20X1], the Investment in [Investment Entity] was presented under non-current assets as "[…]" in the amount of the acquisition costs of [currency] [amount].

17. SER started to request additional information from the Company on [date] [20X2] with a follow-up request on [date] [20X2]. One point raised related to the value of the Investment at [annual reporting period-end] [20X1]. X. ___ provided SER an impairment test for the Investment in [Investment Entity] for the year-end [20X1] valuation on [date] [20X2]. Within this impairment test, X. ___ performed a value in use calculation based on the discounted cash flow method and used financial data for five plan years (**FY**), being FY[20X2] until FY[20X6]. The result of this impairment test was a net present value (**NPV**) for the Investment in [Investment Entity] as per [annual reporting period-end] [20X1] of [currency] [amount] ([currency] [amount]) that indicated no impairment requirement for the carrying amount of [currency] [amount] of X. ___'s investment in [Investment Entity] at the time.

18. Furthermore, X. ___ started consolidation of [Investment Entity] on [first day of the reporting period] [20X2], even though the ownership interest remained […]. X. ___ states three factors that apparently led to the change in the consolidation approach for [Investment Entity] as per [first day of the reporting period] [20X2], as compared to [annual reporting period-end] [20X1]:

- The close working relationship including sharing of offices and co-developing projects between [Investment Entity] and X. ___'s subsidiary [subsidiary];
- The financing of [Investment Entity] that has largely been assumed by X. ___ group entities and/or related parties of X. ___, and;
- Because “certain minority shareholders and Board Members of X. ___ hold minority shareholding positions in [Investment Entity], either directly or indirectly through affiliate entities”.

19. When asked to substantiate these three factors, X. ___ explained, in particular, (i) that the sharing of offices between X. ___'s subsidiary [subsidiary] and [Investment Entity] in fact only started on [date of the second-half-year reporting period] [20X2], (ii) that [Investment Entity]'s financing has largely been covered by B. ___ Inc., which only became a subsidiary of X. ___ on [date of the second-half-year reporting period] [20X2], and (iii) that a minority shareholder of X. ___ has provided financing to [Investment Entity] on [date] [20X2].

20. On [signing date renegotiated options] [20X2], X. ___ signed renegotiated option agreements related to the acquisition of the Investment in [Investment Entity]. The former option 1 had already expired on [signing date renegotiated options] [20X2]. Former option 2 was superseded through the renegotiated options and former option 3 had been replaced by newly agreed options that are described hereinafter. These new options signed on [signing date renegotiated options] [20X2] (**Option A, B, and C**) all have identical terms and conditions and provide for a total additional ownership stake of […]% in [Investment Entity]. In total, a consideration of [currency] [amount] would have to be paid upon exercise of these new options (A, B, and C) and the new call options (A, B, and C) are all valid from [date of the second-half-year reporting period] [20X2] until [date] [20X3]. These three new option agreements (A, B, and C) contain the following terms:

	Signing Date	Seller	Option-Shares	Economic Interest of Option-Shares	Exercise Price Call and Put Option in [currency]	Call-Option Duration	Put-Option Duration
Option A	[signing date renegotia-ted opti-ons] [20X2]	C. ___ Inc.	[quantity]	12%	[amount]	[date of the second-half-year reporting period] [20X2] until [date] [20X3]	[date] until [date][20X3]
Option B	[signing date renegotia-ted opti-ons] [20X2]	D. ___ Inc.	[quantity]	18%	[amount]	[date of the second-half-year reporting period] [20X2] until [date] [20X3]	[date] until [date][20X3]
Option C	[signing date renegotia-ted opti-ons] [20X2]	E. ___	[quantity]	6%	[amount]	[date of the second-half-year reporting period] [20X2] until [date] [20X3]	[date] until [date][20X3]

These new options (A, B, and C) are exercisable at the discretion of X. ___'s board and would, after the exercise of all options, give X. ___ a total […]% share of the voting rights.

21. As a consequence of the proceedings initiated by SER, X. ___ materially restated in its [20X2] FER annual financial statements the carrying amount of [Investment Entity] to [currency] [amount] and retrospectively recorded a corresponding impairment charge of [currency] [amount] as per [annual reporting period-end] [20X1].

22. Furthermore, as an additional consequence of the proceedings initiated by SER, [Investment Entity] was no longer consolidated as of [first day of the reporting period] [20X2] in the [20X2] FER annual and [20X3] FER interim financial statements. X. ___ disclosed in the [20X2] FER annual financial statements that the consolidation of [Investment Entity] as per [first day of the reporting period] [20X2] was erroneous and that the respective correction would also take place in the [20X3] interim consolidated financial statements, which was the case.

3. Considerations

3.1. Missing Impairment of [Investment Entity] in X. ___'s [20X1] FER Annual Financial Statements

23. On [date] [20X2] X. ___ provided SER with an impairment test for the Investment in [Investment Entity] related to its [20X1] FER annual financial statements based on a value in use calculation, as allowed by FER 20/4. However, SER estimates that the value in use calculation contained a mechanical error, implausible aggressive terminal growth rate and other assumptions, and was prepared without due care. Overall, the erroneous test led X. ___ to the wrong conclusion not to recognize a necessary material impairment charge on its [Investment Entity] investment in the [20X1] FER annual financial statements.

3.1.1. Implausible Aggressive Terminal Growth Rate and other Assumptions

24. X. ___ used an enormously aggressive terminal growth rate of 10% in the impairment test for the Investment in [Investment Entity] as per year-end [20X1]. A terminal growth rate of 10% implies that the free cash flow of the [Investment Entity] business after [20X6] would be growing indefinitely, year on year, by 10%.

25. Both FER 20/23 and FER Framework/32 require the use of reliable and probable assumptions in an impairment test in order to avoid presenting distorting or arbitrary information in financial statements.

26. The terminal value is frequently the most significant part of the NPV resulting from a discounted cash flow model. This is particularly the case for a business such as [Investment Entity]’s, which generates very little, or even negative, cash flows during the detailed planning period. On an undiscounted basis, the terminal value of [Investment Entity] amounts to [currency] [lower three-digit amount], compared to a total undiscounted value generated during the 5-year (FY [20X2] – FY [20X6]) planning period of [currency] [low two-digit amount]. Discounted at the rate of [discount rate] used by X. ___ in the impairment test, the terminal value accounts for approximately [currency] [amount] or 88% of the total NPV of [currency] [amount].

27. SER stresses that it is therefore particularly important that the terminal growth rate, which is the key assumption determining the terminal value, is reliable and probable as required by FER 20/23. It is commonly understood in valuation theory that the terminal growth rate cannot be higher than the growth rate of the economy in which a company operates. This is based on the logical assumption that no business will ever be able to outgrow the overall economy into perpetuity.

28. X. ___ failed to substantiate the very aggressive terminal growth rate of 10% used in the impairment test for the Investment in [Investment Entity] as per [annual reporting period-end] [20X1]. No reasonable calculation or relevant external sources stating a 10% growth rate were provided by X. ___, supporting the use of such an enormous terminal growth rate. Furthermore, comparing this aggressive 10% terminal growth rate with the estimation of the International Monetary Fund (IMF) for the [relevant market] (which is the main country of operations for [Investment Entity]) for [20X7] of [low single digit number]% illustrates the implausibility of the used 10% terminal growth rate by X. ___.

29. Changing the terminal growth rate used in the impairment test for X. ___’s Investment in [Investment Entity] as per year-end [20X1] from 10% to the [low single-digit number]% stated above, results in a decrease of the NPV for X. ___’s […] stake in [Investment Entity] to [currency] [amount] instead of the original [currency] [amount]. However, the terminal growth rate was not the only aggressive assumption in the original impairment test. The growth rates in the plan years FY [20X2] to FY [20X6] ranging from [two-digit number]% to [four-digit number]% were also rather aggressive and have not been considered in the error estimation. Reducing or probability-weighting these planned cash flows would also lead to a lower NPV and correspondingly to a higher impairment.

3.1.2. Mechanical Error in the Impairment Test

30. X. ___ based its calculation of the terminal year in its [20X1] year-end value in use calculation for the Investment in [Investment Entity] on the FY[20X5] instead of FY[20X6] plan year. However, finance theory requires the terminal value in a value in use calculation to be based on the terminal plan year used. This correction would by itself, thereby ignoring the adjustments described above, increase the so-called headroom that reflects the difference between the carrying amount in the accounting records and the calculated NPV in an impairment test. Only once this headroom is consumed, does an impairment charge need to be recorded according to FER 20/3. A corresponding correction of the impairment test for [Investment Entity] as per [annual reporting period-end] [20X1] using the assumptions used by the Company, which however as mentioned above are not considered by SER to be realistic, would have increased the NPV for the Investment in [Investment Entity] as per [annual reporting period-end] [20X1] to [currency] [amount] as compared to the original [currency] [amount].

3.1.3. Lack of Due Care in the Process for the Preparation of the Impairment Test

31. X. ___ explained in its answer dated [date] [20X2] that [Investment Entity]'s business plans are prepared by local management and approved by the local board. Furthermore, X. ___'s response dated [date] [20X2] does not mention any approval process or actual approval of [Investment Entity]’s impairment test by the management or the board of X. ___. According to SER, this suggests that no formal approval process or supervision existed regarding [Investment Entity]'s business plans and assumptions used in the underlying data for the impairment test performed as per [annual reporting period-end] [20X1].

32. The submitted minutes of the meetings of the board of directors of X. ___ in [20X1] and [20X2] do not reveal any critical assessment of the impairment tests or their impact on the financial statements of X. ___. According to the minutes dated [date] [20X2], the [20X1] annual financial statements got directly approved. Furthermore, the minutes of the meeting dated [date] [20X2] are the only reference to an assessment of X. ___'s board of directors of the [20X1] annual financial statements.

33. In addition, other impairment tests performed by X. ___ for its remaining investments as per year-end [20X1], whose overall effects are immaterial and were thus not considered by SER in the sanction proposal, contained mechanical errors as well. For instance, one test compared an old NPV to a new NPV of the same project instead of comparing the CGU's NPV to its carrying amount, as would be required by applying a proper impairment test according to FER 20/3. The above illustrates that the shortcomings in X. ___'s processes and controls for performing impairment tests are numerous.

34. The preceding paragraphs demonstrate the missing due care of X. ___ in the preparation of the impairment test of [Investment Entity] for the year-end [20X1]. The very ambitious, not probability-weighted free cash flow growth rates of [two-digit number]% to [four-digit number]% in the first five years, as well as the highly aggressive 10% terminal value growth rate, were neither challenged nor checked by X. ___'s management and demonstrate an inadequate process and the lack of the necessary due care. As a consequence, the valuation of [Investment Entity] has been significantly overstated in the [20X1] FER annual financial statements.

3.1.4. Overall Effect of the Errors in the Impairment Test

35. SER concludes, that the lack of due care in the process of preparing the [20X1] year-end impairment test for [Investment Entity] above caused the errors. The combined correction of these two errors, i.e. using the IMF's growth rate of [low single-digit number]% instead of the implausible aggressive 10% as terminal growth rate and calculating the terminal value based on the last plan year leads to an NPV for X. ___'s Investment in [Investment Entity] as per [annual reporting period-end] [20X1] of a maximum of [currency] [amount] instead of the original [currency] [amount]. As a consequence, a highly material impairment charge has not been recognized in the [20X1] FER annual financial statements of X. ___ was missing in the consolidated balance sheet as well as consolidated income statement of the [20X1] FER annual financial statements.

36. As described, X. ___ restated the [20X1] year-end figures in the [20X2] FER annual financial statements, which resulted in a new impaired carrying amount for [Investment Entity] of [currency] [amount] as per [annual reporting period-end] [20X1]. This amount is significantly below the NPV of [currency] [amount] calculated by SER stated above. However, the terminal growth rate was not the only aggressive assumption in the original impairment test. The growth rates in the plan years FY [20X2] to FY [20X6] ranging from [two-digit number]% to [four-digit number]% were also rather aggressive and have not been considered in the error estimation. Reducing or probability-weighting these planned cash flows would lead to a lower NPV and correspondingly to a higher impairment. Hence, the restatement provided by X. ___ has been deemed reasonable by SER.

    SaKo concurs with the reasoning provided by SER.

37. The following table shows, using the Company's own estimate of the required impairment at [annual reporting period-end] [20X1] of the Investment, the material effect of the restatement in the [20X2] FER annual financial statements of X. ___ of the [20X1] figures:

in [currency]	Original figures for [20X1]	Adjustment	Restated figures for [20X1] in [20X2]	Effect on original figures of [20X1] (original x% too high/low)
Operating result (EBIT)	-[amount]	-[amount]	-[amount]	**80.0% too high**
Result before income tax	-[amount]	-[amount]	-[amount]	**108.8% too high**
Net result	-[amount]	-[amount]	[amount]	**99.6% too high**
Total assets	[amount]	-[amount]	[amount]	**21.5% too high**
Total equity	[amount]	-[amount]	-[amount]	**170.9% too high**

3.2. Erroneous Consolidation of [Investment Entity] in the [20X2] FER Interim Financial Statements

38. According to FER 30/2 subsidiaries are to be consolidated. A subsidiary is a company that is controlled by the parent (FER 30/45). Control is established either by a majority of voting rights (FER 30/46) or by other means, such as contractual arrangements or a majority in the board (FER 30/47). No such means of establishing control as mentioned in the standard were in place for X. ___ over [Investment Entity] during the interim reporting period up to [interim reporting period-end] [20X2].

39. The reasons a) to c) below, which, according to X. ___'s [20X2] FER interim financial statements, were establishing control and triggering consolidation of [Investment Entity] as of [first day of the reporting period] [20X2], are according to SER invalid when assessing control under the FER rules (specifically FER 30/45 to FER 30/47) for the following reasons:

    a) *The close working relationship including sharing of offices and co-developing projects between [Investment Entity] and X. ___'s subsidiary [subsidiary]:*
    X. ___ provided no evidence as to why working relationships and/or the sharing of office space should establish control. Hence, this argument is unsubstantiated in the view of SER. Furthermore, X. ___ stated that the sharing of offices only started on [date of the second-half-year reporting period] [20X2], i.e. only after the end of the interim period presented in the [20X2] FER interim financial statements of X. ___. Therefore, irrespective of whether the working relationship and sharing of offices would be a valid argument regarding control over a subsidiary, an event after the end of the interim reporting period does not trigger consolidation at any date during the interim period.

    b) *The financing of [Investment Entity] that has largely been assumed by X. ___ group entities and/or related parties of X. ___:*
    This referred financing has mainly been provided by B. ___ Inc., an entity that has only been acquired by X. ___ on [date of the second-half-year reporting period] [20X2], i.e. after the interim period end of the [20X2] FER interim financial statements of X. ___ being [interim reporting period-end] [20X2]. Thus, the financing after the balance sheet date by a related party or a subsidiary does not constitute that X. ___ has control over [Investment Entity] in the first half-year of [20X2].

    c) *Because "certain minority shareholders and Board Members of X. ___ hold minority shareholding positions in [Investment Entity], either directly or indirectly through affiliate entities":*
    X. ___ does not control its shareholders, whether minority or majority or any other shareholders, but its shareholders control X. ___. Consequently, X. ___ does not control any companies controlled by its shareholders. Therefore, also this argument does not constitute that X. ___ had control over [Investment Entity] as of [first day of the reporting period] [20X2] or during the first half-year of [20X2].

40. Furthermore, the option agreements that were in place could (help to) establish control through potential voting rights, but only if such options were exercisable during the reporting period in question. Options that become exercisable only after the reporting period cannot be considered in the reporting period to establish control.

41. Due to the short-dated-break-option valid until [end of first month of the reporting period] [20X2], neither significant influence nor control could have existed for X. ___ over [Investment Entity] until the expiration of this option, i.e. on [beginning of the second month of the reporting period] [20X2], as the seller could have revoked the agreement by paying [currency] [amount] at its sole discretion. Moreover, the second option, prevented X. ___ from establishing control before [end of fifth month of the reporting period] [20X2], as it gave the seller a repurchase right that was only cancelled by the new option agreements signed on [signing date renegotiated options] [20X2]. The third option that enabled X. ___ to acquire an additional […]% stake in [Investment Entity] was also replaced by the new option agreements signed on [signing date renegotiated options] [20X2]. However, the latter only became exercisable on [date of the second-half-year reporting period] [20X2],

hence after the interim reporting period ending on [interim reporting period-end] [20X2] of the [20X2] FER interim financial statements. Therefore, both the former option agreements and the recent option agreement do not substantiate control of X. ___ over [Investment Entity] in the first half-year of [20X2].

42. It appears that the above inadequate arguments supporting consolidation of [Investment Entity] during the first-half of [20X2] were supported by X. ___'s board of directors, as it approved the [20X2] FER interim financial statements of X. ___ on [date] [20X2].

43. SER finds, and SaKo concurs, that the insufficient and unfounded argumentation of X. ___, together with the missing challenge of the consolidation assessment regarding [Investment Entity] by X. ___'s management and board of directors for the [20X2] FER interim financial statements lead to the conclusion that the respective process and specific knowledge of the applicable financial reporting standard FER is inadequate at the level of both management and board of directors. Overall, this erroneous process and insufficient knowledge led to wrong and thus unreliable financial statements (contrary to FER Framework/32) that do not give a true and fair view of the issuer's financial position (contrary to FER Framework/6).

44. Subsequent to questions raised by SER, X. ___ confirmed that the consolidation of [Investment Entity] starting [first day of the reporting period] [20X2] in its [20X2] FER interim financial statements was erroneous. X. ___ corrected the erroneous consolidation of [Investment Entity] in the first half-year [20X2] in its [20X2] FER annual and [20X3] FER interim financial statements.

45. In essence, SER states that the inadequate process regarding the assessment of control over [Investment Entity] by X. ___ led to the wrong conclusion regarding the existence of control in the first half-year [20X2] and consequently to the erroneous consolidation of [Investment Entity] starting [first day of the reporting period] [20X2] (contrary to FER 30/2 and FER 30/45-47). This erroneous consolidation resulted in materially erroneous [20X2] FER interim financial statements of X. ___ that did not present a true and fair view of the company (contrary to FER Framework/6) and were thus unreliable (contrary to Framework/32).

46. X. ___ has calculated that the effects of the erroneous consolidation of [Investment Entity] starting [first day of the reporting period] [20X2] on the [20X2] FER interim financial statements of X. ___ to be as follows:

in [currency]	Actual figures in the [20X2] FER interim financial statements	Reversal of [Investment Entity]'s [20X2] interim financial statements	Reversal of the consolidation adjustments regarding [Investment Entity]	Result X. ___ without the consolidation of [Investment Entity]	Total Adjustments[4]	Total Adjustments in % of actual figures (actual figures x% too high/low)
			<u>**Consolidated income statement**</u>			
Total revenue	[amount]	-[amount]	[amount]	[amount]	-[amount]	**12.1% too high**
EBIT	-[amount]	[amount]	[amount]	-[amount]	[amount]	**66.5% too low**
Income tax	-[amount]	-	-	-[amount]	-	**-**
Net result	-[amount]	[amount]	[amount]	-[amount]	[amount]	**64.1% too low**
Basic and diluted earnings per share (in [currency] per share)	-[amount]			-[amount]	-[amount]	**63.2% too low**

[4] Calculated by SER

in [currency]	Actual figures in the [20X2] FER interim financial statements	Reversal of [Investment Entity]'s [20X2] interim financial statements	Reversal of the consolidation adjustments regarding [Investment Entity]	Result X. ___ without the consolidation of [Investment Entity]	Total Adjustments[4]	Total Adjustments in % of actual figures (actual figures x% too high/low)
			Consolidated balance sheet			
Total current assets	[amount]	-[amount]	-	[amount]	-[amount]	**22.5% too high**
Total non-current assets	[amount]	-[amount]	[amount]	[amount]	[amount]	**13.1% too low**
Total current liabilities	[amount]	-[amount]	-	[amount]	-[amount]	**12.1% too high**
Total non-current liabilities	[amount]	-[amount]	[amount]	[amount]	-[amount]	**8.6% too high**
Total equity attributable to owners	-[amount]	[amount]	[amount]	[amount]	[amount]	**144.3% too low**
Non-controlling interests	[amount]	-	-	[amount]	-	**-**
			Consolidated cash flow statement			
Net cash used in / from operating activities	-[amount]			-[amount]	[amount]	**62.4% too low**
Net cash used in / from investing activities	[amount]			-[amount]	-[amount]	**289.6% too high**
Net cash used in / from financing activities	[amount]			-[amount]	-[amount]	**486.5% too high**

3.3. Summary

47. According to SER, X. ___ failed to perform an adequate impairment test for the Investment in [Investment Entity] as per year-end [20X1]. X. ___ consequently failed to recognize a material impairment on the Investment in [Investment Entity] and thus violated the requirements of FER 20/4 and FER 20/23. As a result, X. ___ presented [20X1] FER annual financial statements that were neither in conformity with FER's underlying principle of reliability (FER Framework/32) nor with the fundamental purpose of financial statements to give a true and fair view of the issuer, as set forth in FER Framework/6.

48. In X. ___'s defense it has to be considered that X. ___ corrected and restated the [20X1] figures by recognizing an impairment of [currency] [amount] on [Investment Entity]'s acquisition costs in their [20X2] FER annual financial statements.

49. SER states that X. ___ also failed to adequately assess the existence of control in accordance with FER 30/45-47 over the same Investment in [Investment Entity] in its [20X2] FER interim financial statements. X. ___ consequently erroneously consolidated [Investment Entity] as a subsidiary in its [20X2] FER interim financial statements. As a result, X. ___ presented [20X2] FER interim financial statements that were neither in conformity with FER's underlying principle of reliability (FER Framework/32) nor the fundamental purpose of financial statements to give a true and fair view of the issuer, as set forth in FER Framework/6.

50. In X. ___'s defense it has to be considered that X. ___ corrected this error in its [20X2] FER annual and [20X3] FER interim financial statements where a restatement was made that reversed [Investment Entity]'s erroneous consolidation in the first half-year of [20X2].

51. The Company does not dispute that both the impairment assessment for [Investment Entity] as per year-end [20X1] and the control assessment for [Investment Entity] in the [20X2] half-year report and subsequent consolidation were false. These errors constitute material errors to both the [20X1] FER audited annual and [20X2] FER unaudited interim financial statements of X. ___. These statements were therefore misleading and were not giving a reliable, true and fair view of X. ___'s financial position and financial performance. Furthermore, these errors would have been avoided by a diligent process in the financial statements' preparation and/or with the adequate FER-knowledge of the management and/or board of directors.

4. Sanction

4.1. Severity of breach

52. The annual financial statements are one of the most important instruments for investors to assess and analyze the financial situation of a company. Therefore, it is of the utmost importance to present fairly, in all material aspects, the financial position of a company (see e.g. decision of the Sanctions Commission dated 29 January 2020 (SaKo-RLE-IV/18), number 44; dated 13 August 2013 (SaKo 2013-AHP-I/12), number 33; and dated 28 June 2012 (SaKo 2012-AHP-II/11), number 56).

53. The error in the [20X1] FER audited annual financial statements authorized for issue and approved by its auditors on [date] [20X2] is **material**. There is a significant impairment expense missing that also significantly affects the balance sheet. Due to this error in the [20X1] FER annual financial statements, the net result has been overstated by 99.6%, total assets have been overstated by 21.5%, and total equity by 170.9%. The erroneously performed impairment test and the resulting missing impairment expense for X. ___'s Investment in [Investment Entity] as per [annual reporting period-end] [20X1] are clear violations of the applicable accounting standard, FER.

54. The error in the [20X2] FER unaudited interim financial statements authorized for issue on [date] [20X2] and published on [date] [20X2] is **material**. The erroneous consolidation of [Investment Entity] starting [first day of the reporting period] [20X2] materially affects the whole [20X2] FER interim financial statements. Due to this error, in the [20X2] FER interim financial statements the net loss has been overstated by 64.1%, basic and diluted loss per share have been overstated by 63.2%, total equity attributable to X. ___'s owners has been understated by 144.3%, net cash used from operating activities has been overstated by 62.4%, and net cash used in / from investing as well as from financing activities have been overstated by 289.6% and 486.5%. This erroneous consolidation is a clear violation of the applicable accounting standard, FER.

55. By overstating X. ___'s Investment in [Investment Entity] in the [20X1] FER annual financial statements and by erroneously consolidating [Investment Entity] in the [20X2] FER interim financial statements, both mentioned financial statements were neither reliable nor presenting a true and fair view about X. ___'s financial position, and represent serious breaches of the applicable accounting standard, FER.

4.2. Degree of fault

56. The LR require issuers to ensure compliance with the LR, additional rules, and related implementing decrees at all times (cf. Art. 60 LR). In the present case, it should be noted that the issue at stake is the sanctioning of a legal entity and not of a natural person. The issuer shall be sanctioned if it is accused of not having taken all necessary and reasonable organizational precautions to prevent a breach of the obligations entered into under the LR. Accordingly, the assessment of fault is performed

according to largely objective standards. The conduct of the natural persons or bodies acting on behalf of the issuer is attributed to the issuer (see decisions of the Sanction Commissions dated 29 January 2020 (SaKo-RLE-IV/18), number 48; dated 8 October 2018 (SaKo 2018 SaKo-RLE-IV/17), number 30; dated 14 April 2015 (SaKo 2015-AhP-I/15), number 19; dated 30 July 2010 (SaKo 2010-CG-II/10, SaKo 2010-MP-I/10), number 13; sanction notice of SIX Exchange Regulation AG dated 20 December 2019 (SER-RLE-III/19), number 32; dated 28 November 2017 (SB-RLE-III/17), number 39; dated 20 June 2016 (SB-RLE/II/16), number 51; dated 12 August 2013 (SER-KTR-FOR-I/13), number 28; dated 4 February 2013 (SER-MT II/12/SER-AHP I/12/SER-Listing I/12), number 103).

57. Anyone who violates the relevant provision consciously acts intentionally. An issuer acts with conditional intent if it does not directly intend to violate an obligation, but at least accepts the likelihood of a violation (see decisions of the Sanctions Commission dated 2 August 2019 (SaKo AhP-I/19), number 51; dated 28 June 2012 (SaKo 2012-AHP-II/11), number 46; sanction notice of SIX Exchange Regulation AG dated 20 December 2019 (SER-RLE-III/19), number 33; dated 28 November 2017 (SB-RLE-III/17), number 40; dated 20 June 2016 (SB-RLE/III/16), number 49; dated 18 April 2016 (SB-RLE/I/16), number 30; dated 11 October 2013 (SER-AHP-I/13), number 48; dated 12 August 2013 (SER-KTR-FOR-I/13), number 26; dated 4 February 2013 (SER-MT II/12/SER-AHP I/12/SER-Listing I/12), number 101).

58. A person who has not considered the consequences of his conduct or has not taken them into consideration due to carelessness acts negligently (see decisions of the Sanctions Commission dated 29 January 2020 (SaKo-RLE-IV/18), number 49; dated 2 August 2019 (SaKo AhP-I/19), number 52; dated 8 October 2018 (SaKo 2018 SaKo-RLE-IV/17), number 31; dated 13 August 2013 (SaKo 2013-AHP-I/12), number 36; sanction notice of SIX Exchange Regulation AG dated 20 December 2019 (SER-RLE-III/19), number 34; dated 28 November 2017 (SB-RLE-III/17), number 41; dated 20 June 2016 (SB-RLE/II/16), number 50; dated 18 April 2016 (SB-RLE/I/16), number 31; dated 21 August 2014 (SER-MP-I/14), number 22; dated 11 October 2013 (SER-AHP-I/13), number 48; dated 12 August 2013 (SB-KTR-FOR-I/13), number 27; dated 4 February 2013 (SER-MT II/12/SER-AHP I/12/SER-Listing I/12), number 102).

59. In the assessment of the degree of fault, the consistent practice is to expect from listed companies, compliance with stock exchange regulations without further ado. The responsible employee must be familiar with all relevant regulations, including the applicable accounting standard, comments, and practice of the stock exchange bodies (see decisions of the Sanction Commission dated 29 January 2020 (SaKo-RLE-IV/18), number 50; dated 2 August 2019 (SaKo AhP-I/19), number 53; dated 14 April 2015 (SaKo 2015-AHP-I/15), number 26; dated 13 August 2013 (SaKo 2013-AHP-I/12), number 37). Based on the issuers' duty of care, every issuer is expected to be familiar with the applicable stock exchange rules, commentaries and practice of the judicial bodies. Any breach of the rules and regulations must raise a presumption of negligence of the issuer in failing to discharge its duty of care (see decision of the Sanctions Commission dated 29 January 2020 (SaKo-RLE-IV/18), number 50; cf. decisions dated 2 August 2019 (SaKo-AhP-I/19), number 53; sanction notice of SIX Exchange Regulation AG dated 20 December 2019 (SER-RLE-III/19), number 35; dated 28 November 2017 (SB-RLE-III/17), number 42; dated 11. October 2013 (SER-AHP-I/13), number 49; dated 4. February 2013 (SER-MT II/12/SER-AHP I/12/SER-Listing I/12), number 104).

60. Neither X. ___'s impairment test of the Investment in [Investment Entity] as per year-end [20X1] nor its assessment of control and the resulting conclusion on the consolidation of [Investment Entity] in the [20X2] interim financial statements are in accordance with FER (specifically FER 20 and FER 30). Therefore, the respective financial statements are not reliable and do not give a true and fair view of the financial position and performance of the Company (contrary to FER Framework/6 and FER Framework/32).

61. As set out above, X. ___'s procedures for both testing the Investment in [Investment Entity] as per [annual reporting period-end] [20X1] for impairment and for analyzing the existence of control over [Investment Entity] in the first-half [20X2] lacked the necessary due care and suggest a lack of the necessary expertise regarding the applicable accounting standards for the preparation of financial statements. The impairment test contained basic mechanical errors as well as assumptions that were clearly recognizable as improbable and unreliable. The assessment of control was performed based on criteria that were obviously not in line with FER.

62. X. ___'s behavior must therefore be qualified as **grossly negligent**.

4.3. Sensitivity to sanctions

63. When determining the sanction, the impact of the sanction on the party concerned has to be taken into account. In order to assess the impact, the economic performance of the issuer is considered. An issuer with a lower economic performance will tend to be more affected by the same fine than a company with a comparatively higher economic performance. For the determination of the impact, economic key figures can be taken into consideration, e.g. EBIT, net income, operating cash flow, cash and cash equivalents, or equity (see decisions of the Sanctions Commission dated 29 January 2020 (SaKo-RLE-IV/18), number 54; dated 2 August 2019 (SaKo AhP-I/19), number 68; dated 8 October 2018 (SaKo 2018 SaKo-RLE-IV/17), number 39; dated 28 June 2012 (SaKo 2012-AHP-II/11), number 63 et seq., and dated 8 December 2011 (SaKo 2011-AHP-I/11, SaKo 2011-CG-I/11), number 37).

64. In the latest [20X3], [20X2] and [20X1] FER consolidated annual financial statements of X. ___, the Company reports the following economic performance and financial figures:

in [currency]	[20X3] FER annual financial statements	[20X2] FER annual financial statements	[20X1] restated FER annual financial statements
Net cash used in / from operating activities	[amount]	-[amount]	[amount]
Total cash flow for the period	-[amount]	-[amount]	[amount]
Cash and cash equivalents as per balance sheet date	[amount]	[amount]	[amount]
EBIT	-[amount]	-[amount]	-[amount]
Net profit/(loss)	[amount]	-[amount]	-[amount]
Total equity	[amount]	-[amount]	-[amount]

65. On [date] [20X4], X. ___ published a press release on its website, according to which the Bankruptcy Court of the [place] has declared bankruptcy over the Company. The decision relates to a claim for […] by […] in the amount of [currency] [amount]. The existence of the claim is currently subject to a civil proceeding in [place]. The claim is disputed by the Company. On [date] [20X4], X. ___ informed the public that the Appeals Court of [place] has suspended the bankruptcy procedures.

66. In view of the economic ratios described above and considering the bankruptcy proceedings, the sensitivity to sanctions of the Company is determined to be **very high**. Therefore, the Sanctions Commission agrees to a substantially lower sanction compared to prior sanctions with the same severity of breach of regulations and degree of fault.

4.4. Previous Sanctions

67. In calculating the sanction, any previous sanctions of the last three years can be taken into account (Ciph. 2.6 para. 4 RP). In favor of the issuer, it should be noted that no sanctions were imposed on X. ___ during this period.

4.5. Behavior after the Violations

68. In favor of X. ___ it has to be noted that X. ___ restated and impaired the carrying amount of [Investment Entity] to [currency] [amount] as per [annual reporting period-end] [20X1] in its [20X2] FER an-

nual financial statements. Within this restatement, the overvaluation by [currency] [amount] is recognized and presented as impairment of investments.

69. Furthermore, in note […] of the [20X2] FER annual financial statements, X. ___ confirms the erroneous consolidation of [Investment Entity] as per [first day of the reporting period] [20X2] and states that the corresponding correction will also take place in the [20X3] interim consolidated financial statements, which was the case. Therefore, no more erroneous consolidation of [Investment Entity] in the first half-year [20X2] is visible in the [20X2] FER annual and [20X3] FER interim financial statements.

5. Conclusion

70. Art. 61 para. 2 LR provides that in determining the sanction to be imposed, due consideration must be given, in particular, to the severity of the breach and to the degree of fault. When setting the level of fines, the Sanctions Commission also takes into account the impact of the sanction on the party concerned. Art. 61 para. 1 LR provides for the possibility to impose a fine, which may amount up to CHF 1 million (in case of negligence) and up to CHF 10 million (in case of wrongful intent).

71. Considering that X. ___ acted with **gross negligence** which resulted in **serious breaches** of the applicable accounting standard FER and taking into account the **high impact** of the sanction on X. ___ and its **positive behavior after the violations**, SaKo imposes a **fine of CHF 40'000** on the company in accordance with Art. 61 para. 1 number 2 LR.

72. In case of sanction proceedings, charges are determined based on the expenditure incurred by the plaintiff (SER), adopting an hourly rate of CHF 300 per person (Ciph. 3.7 in connection with Ciph. 4.1 of the List of Charges Regulatory Bodies[5] (**LocRB**)). In the present case, charges of SER amount to CHF […].

73. The costs of the Sanctions Commission amount to CHF […] and shall be borne by X. ___ as well.

[Place], 18. September 2020

The Chairman:	The Secretary:
[Sig.] Chairman	[Sig.] Secretary

[5] List of Charges Regulatory Bodies (LocRB) dated 11 September 2019, entry into force 1 January 2020