Proposed Provisions regarding Insider Lists and Management Transactions – Critical View on a Proposed Shift in Paradigm

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The draft changes proposed in the consultation on the amendment to the Financial Market Infrastructure Act (FMIA) seek to transfer issuer obligations from self-regulation by the stock exchange(s) to the FMIA and, associated with such transfer, the assignment of competencies from Swiss stock exchanges to FINMA. Among these issuer duties is the obligation to report management transactions. In addition, an explicit issuer obligation to maintain insider lists is introduced into the FMIA. The proposed changes would, if enacted, constitute a shift of paradigm in issuer regulation in Switzerland: The tradition of self-regulation of stock exchanges would cave in favor of governmental supervision along the EU model.

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1) Introduction

The draft legislation proposed by the Swiss Federal Council to amend the Financial Market Infrastructure Act (Draft-FMIA) includes several obligations of Swiss issuers of securities that, up until now, were governed by the relevant self-regulatory framework of the respective Swiss stock exchanges. Among these duties is the obligation to report management transactions (art. 37c Draft-FMIA) which is sometimes also referred to as reporting of "directors' dealings". The rule is intended to provide market participants with information on the trading by "insiders", i.e. members of the management and the board of directors of an issuer. In addition, the proposed revision of FMIA also includes a duty to prepare insider lists (art. 37a Draft-FMIA). Under the self-regulatory framework of Swiss stock exchanges such a duty is currently not expressly stipulated, but clearly considered "best practice" and a pre-requisite of a legitimate postponement of the disclosure of price-sensitive (ad hoc relevant) information by an issuer. However, non-compliance with such duty is currently not directly sanctioned.

2) Self-regulation vs. government regulation

On a more general note, we question the plan to abolish self-regulation in the area of issuer obligations and advocate retaining the current self-regulatory regime. In our view, several compelling reasons speak in favor of the current tried and tested system. Furthermore, the change of system would de facto largely abolish the concept of self-regulation laid down in art. 27 FMIA. Due to its history and its lack of experience and affinity in this area, we also do not consider FINMA to be suitable for supervising issuers.

Self-regulation in this area has proven its worth and the existing regulation was even considered equivalent by the EU. The EU Commission refused to recognize Swiss regulation not because of the technical regulation in the FMIA or the self-regulation by the stock exchange, but because the framework agreement between Switzerland and the EU did not materialize. Furthermore, there are numerous other jurisdictions that also recognize the principle of self-regulation, not least the United States – the Swiss regime is therefore not unique.

From an enforcement perspective in particular, we believe that self-regulation and the sanctioning of issuers through contractual penalties provided for in the listing rules, among other things, are much more suitable than the instruments of supervisory law. Criminal law (including administrative criminal law) focuses in particular on the individual liability of natural persons. However, wrongdoing in maintaining insider lists or the publication of management transactions is usually the result of "operational accidents" rather than the conspiracy of criminal employees. Accordingly, the penalization of individuals due to violations of issuer obligations seems disproportionate and inappropriate to us, as the decision as to whether and when an insider list is prepared and maintained, for example, is not made by one person, but is usually decided by a committee.

Instead of supervising new issuers, we believe that FINMA's resources would be better used if it were to focus on the supervision of financial institutions and intermediaries currently supervised by FINMA instead of expanding the scope of state supervision. If self-regulation is being questioned, which in our view should not be the case, this paradigm shift should be prioritized in the core areas of financial market supervision, e.g. in the supervision of financial institutions and financial intermediaries, instead of making issuers that were not previously supervised by FINMA (except to a limited extent like all other market participants in the area of combating market abuse) subject to FINMA supervision.

3) Insider Lists (art. 37a Draft-FMIA)

The scope of the obligation to maintain insider lists is aimed at issuers on a Swiss stock exchange or a Swiss DLT trading facility and their agents. The same applies under EU law, where issuers and persons acting on their behalf or for their account are obliged to maintain an insider list. It should be noted that the issuer or the person acting on its behalf or for its account is not released from its obligation if or to the extent that any of the other addressees of the duty maintains such list.

Art. 37a para. 3 Draft-FMIA stipulates that the Federal Council may provide for exceptions to the obligation on grounds of proportionality. However, further details are still lacking. In our opinion, the fact that lawyers may also be considered "agents" in the meaning of art. 37a Draft-FMIA triggering the duty to maintain such list is problematic. The question arises as to what extent attorney-client privilege typically precludes the disclosure of such insider lists (being an information that has been entrusted to the attorney because it has

provided typical legal services). It remains to be seen whether the respective authorities will use attorneys and other service providers benefitting from a privileged information exchange as "civil servants" and requesting the disclosure of insider lists.

While the EU has a prescribed format for insider lists and requires that they be kept electronically (art. 2 of the Commission Implementing Regulation (EU) 2016/347), there is no corresponding regulation in the draft legislation. The modalities will still have to be determined by the Federal Council, even though it seems highly likely that the implementing rules will require the list to be kept electronically.

The insider list must include all persons who have authorized access to insider information. The wording is similar to that of EU legislation. EU legislation specifies that the persons to be included on the insider list are those who, on the basis of an employment contract or otherwise, perform tasks for the issuer that give them access to insider information, such as advisors, accountants or rating agencies (art. 18 para. 1 let. a MAR). The content requirements for the entries on the insider list remain open at present and have yet to be determined by the Federal Council. In the EU, art. 18 para. 3 MAR provides certain minimum requirements (identity of all persons including the national identification number, reason for inclusion, date and time when this person received the information, date of creation of the list). In case the proposed changes will be enacted, we would encourage the government – who will be competent to draft the implementing legislation – to abstain from making (too many) formal requirements. Such formal requirements include e.g. the obligations that the persons covered must provide written acknowledgement (art. 18 para. 2 MAR).

While EU law stipulates a minimum retention period of 5 years (art. 18 para. 5 MAR) and the lists are to be destroyed after 5 years due to data protection regulations, the draft legislation provides for a minimum retention period of 15 years. This period is allegedly warranted for the purpose of criminal prosecution according to the draft proposal. In our view, the fifteen-year retention requirement is disproportionately long, particularly in comparison with the EU. It goes significantly further than the general document retention requirement under art. 958f of the Swiss Code of Obligations (see also art. 730c para. 1, art. 747 of the Swiss Code of Obligations) or the retention requirements of art. 7 para. 3 of the Anti-Money Laundering Act and the corporate law obligations to identify the beneficial owners (art. 686 para. 5, art. 697f para. 3 of the Swiss Code of Obligations).

Keeping insider lists is already considered best practice and enables issuers and their advisors to prove that the disclosure of inside information was made in accordance with art. 128 FMIO and that they have taken appropriate measures to ensure the confidentiality of inside information in connection with a postponement in ad hoc publicity. We, therefore, consider a corresponding explicit obligation to be redundant and, in particular for small and medium-sized issuers, to be disproportionately formalistic. In addition, the Draft-FMIA stipulates that all issuers of securities on a Swiss stock exchange or a Swiss DLT trading facility are obliged to maintain such insider lists. In the event that this requirement

is maintained, we believe, in the interests of proportionality, that it should be limited to companies that have issued equity securities.

The draft legislation provides for criminal liability for violating the obligation to maintain insider lists. Not only the intentional breach of the obligation but also mere negligence is punishable. While the breach of the obligation is only punishable by a fine, which means that it is just a contravention, the provision provides for a fine of up to CHF 500,000 or 100,000 in case of negligence resulting in an entry in the criminal record and potentially further consequences. Before 2018, the Swiss parliament explicitly rejected criminal negligence under the FinSA. Punishment for negligent behavior in such an administrative matter seems disproportionate in view of the above. In case of any enforcement proceedings, issuers that fail to maintain a proper insider list are already today factually disadvantaged by a failure to meet the burden of appropriate measures to ensure the confidentiality – this by itself is in our view incentive enough to maintain state-of-the-art insider lists. Further, many jurisdictions, including the United States, do not require issuers to maintain such lists. All these reasons lead to the conclusion that punishment of negligent behavior should be dropped in our opinion.

4) Reporting of Management Transactions (art. 37c Draft-FMIA)

Art. 37c Draft-FMIA primarily applies to transactions conducted by the board of directors and senior management of companies with securities traded on a Swiss stock exchange (or a Swiss DLT trading system) in such securities. Transactions that involve trading in securities of the listed company or in derivatives with any such securities as underlying are generally reportable and will be published indicating the generic function (e.g. member of management) but neither the specific role nor the name of the person trading.

The federal government enacting any implementing legislation would yet have to determine the form in which the notification is to be made. In the EU, the use of a form in accordance with the Commission Delegated Regulation (EU) 2016/532 is required.

The exact content of such a report would also have to be determined by the government. It is clear from the explanatory report that the transactions will have to be stated in full, with it being explicitly stated that the name and job title must also be published. This contrasts the existing regimes of the stock exchanges where such information must be provided to the stock exchange, but does not form part of the publicly disclosable information. In the EU, the name of the person, the reason for the report, the name of the relevant issuer, a description and identifier for the financial instrument, the type of transaction, the date and place of the transaction, and the price and volume of the transaction must be stated. We do not see any added value for the market in naming the person and would recommend removing this public disclosure item.

The persons covered include members of the board of directors and senior management of a company, as well as persons close to them. The group of persons

subject to reporting requirements under Swiss law would therefore be less extensive than under EU law. Under EU law, all persons who perform management tasks are subject to reporting requirements. Such persons do not necessarily have to be members of the management; it is sufficient if they make decisions that influence the future development of the company. However, we welcome the proposed restriction to formal members of the board of directors and the C-level management.

EU legislation stipulates that issuers must inform their managers in writing of their reporting obligation. It is also required that the issuer creates a list of the managers and close persons. Furthermore, persons discharging executive responsibilities must also inform those closely associated with them in writing of their reporting obligation and keep a copy of such notification (art. 19 para. 5 MAR). Whether such a formal rule would also be implemented under Swiss law remains to be determined by the government if the proposed changes pass parliament.

EU law requires that persons who carry out management responsibilities and who perform a relevant transaction of their own account must report this to the issuer without delay and at the latest three business days after the date of the transaction (art. 19 para. 1 MAR). The issuer, in turn, must ensure that the information reported in accordance with art. 19 para. 1 MAR is made public without delay and no later than three business days after the transaction (art. 19 para. 3 MAR).

Pursuant to art. 37c para. 1 Draft-FMIA, the members of the board of directors and the senior management, as well as persons closely associated with these members, must report relevant transactions to the company within two trading days. Art. 37c para. 2 Draft-FMIA then stipulates that the company must report the notification received within three trading days. The stock exchange must then publish the report "as soon as possible" and forward it to FINMA. These deadlines correspond to the current regulations of the Swiss stock exchanges and seem appropriate to us.

In addition, the government would be authorized under art. 37c para. 5 Draft-FMIA to mandate blackout periods for management transactions. The EU also has a corresponding regulation that provides for a period of 30 calendar days prior to the publication of an interim report or an annual report during which no more proprietary transactions may be carried out (art. 19 para. 11 MAR). Exceptions are possible (art. 19 para. 12 MAR). The establishment of blackout periods already corresponds to best practice in particular because these periods de facto have to be disclosed in a listed companies corporate governance report (de jure it is a comply or explain regime). To our knowledge, trading bans during these periods are generally observed and do not lead to difficulties in practice. In light of this, we generally oppose the legal codification of such blackout periods.

Art. 149a Draft-FMIA also provides for criminal liability under art. 37c Draft-FMIA for both intentional and negligent breaches, punishable by a fine of up to CHF 500,000

or 100,000 respectively. It follows from the explanatory report that both the failure by the individual to report and the failure by the company to publish will be punishable. The sanction is thus likely to be imposed on the company as well as on the members of the board of directors and the senior management who are subject to the reporting requirement, as well as on persons close to these members. In our opinion, this represents a questionable broadening of the penalization of individuals, particularly in view of the penalization of negligence, as well as the amount of the fine and the resulting entry in the criminal record.

Should the management transactions be transferred from the listing rules of the stock exchanges to the FMIA (which we question), we believe that the legal regulation should be limited to equity securities, as is the case in the current regimes of the Swiss stock exchanges.

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