Content

The Market newsletter addresses topical matters concerning interpretations, regulation, as well as supervisory findings relating to listed companies' disclosure obligation, financial reporting enforcement, securities trading and insider issues. The newsletter is published by FIN-FSA's Supervision of Markets and Conduct of Business Department.

Financial reporting stakeholders in breakfast meeting discussion

On 30 October 2018, IFRS Enforcement organised a breakfast meeting to discuss the current state and future of IFRS reporting. In addition to Erkki Liikanen, the new Chair of the IFRS Foundation Trustees, individuals representing the academic sector, financial reporting regulation and business spoke on the theme.

The Financial Supervisory Authority’s IFRS Enforcement organised a breakfast meeting with **Erkki Liikanen**, the new Chair of the IFRS Foundation Trustees, on 30 October 2018. The aim of the event was to acquaint Finnish financial reporting stakeholders with the new Chair. Five different parties gave prepared statements, which formed the basis for discussion.

Erkki Liikanen spoke about the IFRS Foundation Trustees’ Johannesburg meeting and highlighted the European Commission’s fitness check survey, in which the Commission aims to assess whether current financial reporting regulation is, taken as a whole, appropriate, effective, relevant and efficient. The IFRS Foundation discussed the results of the survey with the Commission at the end of November.

Erkki Liikanen. Photo: Financial Supervisory Authority

In the survey, the parties were asked about the ‘carve-in’ approach, in which additional requirements supporting Europe’s long-term goals would be added to the requirements of the IFRS Standards. The European Securities and Markets Authority (ESMA) has been opposed to the carve-in approach, as this would provide the basis for creating an EU-IFRS.

In addition, Liikanen noted the challenges associated with the adoption of IFRS 17 Insurance Contracts. The insurance industry has raised concerns when the results of the impact analysis included in the standard’s adoption process have been assessed in the European Union. The insurance industry has expressed its concerns by letter both to the IASB and to EFRAG, which is assisting the European Union in the enforcement of the standard.

At the meeting, Professor **Juha-Pekka Kallunki** spoke from an academic perspective, explaining for whom and for what purpose IFRS financial statements are prepared. Initially, regulation targeted companies seeking funding on the international markets. The application of IFRSs requires financial theoretical knowledge, and their principle-based approach means that they are challenging; national accounting philosophy affects their application.

Nevertheless, a number of studies show that the application of IFRSs is beneficial from a capital market perspective, although country-specific factors need to be taken into account. Additional benefit arises to investors if enforcement is effective. The need for balance sheet-based financial statement information has decreased, however, and income statement-based information is increasingly important. One of the major challenges is the reliance of current financial reporting regulation on the business models of the industrial age, where the significance of tangible assets is emphasised over intangibles.

Timo Kaisanlahti, Chief Specialist, Ministry of Economic Affairs and Employment spoke on IFRS and Finland’s national financial reporting regulation. The Ministry has launched a project aimed at taking forward national financial reporting regulation. The current Accounting Act allows certain assets and capital to be treated in accordance with IFRSs.

Kaisanlahti suggested that the current model, where the financial statements of the listed parent company are drawn up in accordance with the Accounting Act and consolidated financial statements in accordance with IFRS, would be transferred to a model in which the parent's financial statements are also prepared, appropriately adjusted, in accordance with IFRS. The adjustment would mean that items affecting the calculation of taxable income would still be treated in accordance with national requirements. The objective of the new model would be to facilitate the financial reporting of listed companies.

Tore Ahlberg (vas.), Juha-Pekka Kallunki, Netta Mikkilä, Erkki Liikanen, Eva Kaukinen and Timo Kaisanlahti. Photo: Financial Supervisory Authority.

Tore Ahlberg, Vice President, Nordea Plc and **Eva Kaukinen**, Vice President, Group Controller, Kesko Corporation spoke on the application of IFRSs. Both considered that, despite the challenging nature of their application, IFRSs produce better financial statement information. Ahlberg also highlighted the benefits and challenges of IFRS reporting. Of the benefits, he mentioned, among other things, the uniform reporting language, which facilitates international comparison of banks' financial statements, and regulation of Finnish banks' separate financial statements, which has been to a large extent adjusted to the requirements of IFRS regulation. On the other hand, as challenges he mentioned, for example, official reporting and the reconciliation of its interpretation guidelines with the freedom of choice and materiality permitted by IFRS reporting. In addition, taxation still does not allow full application of IFRS requirements in separate financial statements.

In her contribution, Kaukinen stated that the most recent reforms of standards (IFRS 15, IFRS 9, and IFRS 16, which enters into force on 1 January 2019) have been exceptionally important changes. They have required significant changes to systems or completely new systems, and so costs have arisen from their introduction. In interpreting the application of the new standards, the significance of management judgment has been underlined. It is positive that the new standards have increased discussion between financial reporting and business functions. Kaukinen pointed out investors are interested in a company's value, i.e. capacity of the business to generate cash flow.

Netta Mikkilä, Partner, PwC exercised audit firms' opportunity to speak at the breakfast meeting. As IFRSs are applied in 166 countries, they constitute a global framework for global markets. Mikkilä emphasised the correct application of IFRSs, which creates genuinely comparable information. Correct application requires the correct reading, understanding and interpretation of a standard's requirements. The goal for all financial reporting stakeholders – regulators, preparers of financial statements, auditors and enforcers – is to build market confidence. Mikkilä highlighted the future challenges of financial reporting, such as digitalisation as well as the development of technology and global capital markets.

The following points emerged from the discussion that followed the speakers' contributions

- to achieve uniform application, correct implementation of enforcement and regulation is essential
- the company's responsibility in applying principle-based requirements underlines the business judgment exercised by management, and this judgment should be documented
- After the introduction of new standards, the IASB should assess whether they have genuinely brought additional benefit to investors compared to the costs arising from them.
- a particular challenge to uniform application might arise in a multinational company where different countries' national accounting philosophies will exert a background influence.
- tax obstacles should be dealt with to enable the preparation of separate financial statements in accordance with IFRSs.
- cash flow statements contain significant information for investors.

For further information, please contact

Virpi Haaramo, Senior Accounting Expert, tel. +358 9 183 5355.

Questionnaire for audit committees of public-interest entities

The Committee of European Auditing Oversight Bodies (CEAOB) has decided to conduct an audit committee questionnaire. The purpose of the questionnaire is to survey the current performance of audit committees in Europe and to promote the implementation of EU audit regulations. The survey will be conducted by national competent authorities.

The Finnish Patent and Registration Office (PRH) is the competent authority on auditing oversight in Finland and a member of the CEAOB. Under the EU Audit Regulation, auditing oversight bodies must regularly monitor the developments in the market for providing statutory audit services to public-interest entities (PIEs). The Financial Supervisory Authority (FIN-FSA), in turn, is the competent authority in assessing and monitoring the performance of audit committees. For these reasons, the PRH's auditing oversight unit and the FIN-FSA collaborated in conducting the questionnaire in January 2019.

Audit committees promote the quality of financial reporting and auditing

The quality and independence of auditing, as well as increased confidence in financial reporting, are a common interest of audit committees and supervisors. Audit committees are significant in improving the quality of financial reporting and play a key role in supporting high quality auditing. The audit committees form a critical and independent view of the matters they consider. Due to the nature of the matters considered by audit committees and under the requirements of the EU Auditing Directive, the majority of committee members must be independent of the entity and no member of the audit committee may participate in the day-to-day management of the entity. In addition, members of the audit committee must as a whole have competence relevant to the sector in which the audited entity is operating and at least one member must have competence in accounting and/or auditing.

The Auditing Directive sets for audit committees, in particular, significant audit-related tasks. The audit committee monitors the performance of the audit and the independence of the auditor/audit firm, particularly with regard to non-audit services provided by them to the audited entity, and prepares a proposal for a decision on the selection of the auditor. In addition, the audit committee promotes sound corporate governance. It monitors the entity's financial reporting process and the effectiveness of risk management systems and internal auditing.

Target group of the questionnaire

The role of PIEs' audit committees has strengthened following the entry into force of the EU Auditing Directive in 2016. In Finland, provisions on audit committees have been added to the Limited Liability Companies Act and special acts. If there is no audit committee, the Board of Directors as a whole handles the tasks of the audit committee or delegates them to some other body to handle. The target group of the questionnaire is an extensive group of PIEs, as defined by the Accounting Act, as well as certain financial sector actors. It is planned that nearly all equity issuers, bond issuers, credit institutions, pension insurance companies and other insurance companies will participate in the questionnaire.

Practical implementation of the questionnaire

For the audit committee survey, the CEAOB has prepared a questionnaire form, which has questions on audit committees' performance and obligations. National competent authorities may add to the questionnaire issues of importance for their own work. The questions prepared by the CEAOB address the following topics

- Oversight of the audit function
- Independence including the prior approval of permitted non-audit services
- Auditor selection process
- Oversight of the financial reporting process
- Oversight of the internal quality control and risk management systems
- Audit committee composition and skills
- Interaction with the administrative or supervisory body.

The survey is conducted in Finland as an electronic questionnaire, so it is easy to respond to; for most of the questions, the most suitable option need only be selected. The questionnaire should be answered no later than March 2019. The information received is confidential. A summary of the responses received will be sent to the CEAOB. This summary will not contain the information of individual respondents. In 2019, the CEAOB will compile and publish a summary the results of the responses of various countries' supervisory authorities.

Questionnaire will benefit both supervisors and audit committees

The questionnaire will help PRH and the FIN-FSA to fulfil their statutory duties. The responses will help supervisory authorities understand how audit committees work in Finland and what challenges they face when applying the new requirements. Hopefully, the questions also help audit committees assess and develop their own performance, particularly from the perspective of applying the new audit regulations.

Accounting Act (30.12.2015/1620) chapter 1 section 9

In Finland, public-interest entities refer to

1. a Finnish entity which has issued a share, bond or another security admitted to trading on a regulated market referred to in chapter 2, section 5 of the Securities Market Act (746/2012);
2. a credit institution referred to in chapter 1, section 7 of the Act on Credit Institutions (610/2014); and
3. an insurance company referred to in chapter 1, section 1 of the Insurance Companies Act (521/2008)

EU Audit Regulation, Article 27(1)(c) Monitoring market quality and competition

The competent authorities designated under Article 20 (1) and the European Competition Network (ECN), as appropriate, shall regularly monitor the developments in the market for providing statutory audit services to public-interest entities and shall in particular assess the following:

c) the performance of audit committees

Act on the Financial Supervisory Authority (12.8.2016/642), section 50 (i) Acting as the competent authority for auditing of public-interest entities

The Financial Supervisory Authority acts as the competent authority, in accordance with Article 20 (2) of the EU Audit Regulation, in assessing and monitoring the performance of audit committees, as referred to Article 27 (1) (c) of the Regulation.

For further information, please contact

Pekka Parviainen, Auditing Expert, tel. +358 9 183 5254.

Disclosure of interests and conflicts of interest concerning investment recommendations

The FIN-FSA has received a number of questions on regulations related to investment recommendations and their interpretation. The questions mainly relate to the scope of regulation – particularly the obligation for analysts and other investment experts to disclose their interests and conflicts of interest concerning the financial instruments to which analyses and recommendations relate.

Article 20 of the Market Abuse Regulation (596/2014, MAR) and the associated Commission Delegated Regulation (958/2016) impose disclosure and code of conduct obligations on persons and entities that provide investment recommendations. In addition, the European Securities and Markets Authority (ESMA) has issued a number of Q&A interpretations on issues related to investment recommendations. The main objective of the obligations is to seek to ensure that recommendations are presented in an impartial manner and that interests and conflicts of interest concerning the financial instruments to which recommendations relate are disclosed in connection with them.

What is an investment recommendation?

'Investment recommendation' means information, intended for distribution channels or for the public, recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or issuers. Such explicit recommendations are, for example, buy, hold and sell recommendations. Implicit recommendations can be made, for example, by indicating a target price or by other means.

In assessing whether an investment recommendation under the regulations is involved, the content of the recommendation and whether the recommendation is intended for distribution channels or the public are significant. Information provided to the public orally or electronically, such as by telephone, email or chat channels, may also be covered by the provision if the recommendation contains an explicit or implicit recommendation or investment suggestion concerning a financial instrument or issuer.

Investment advice where a customer is given an individual recommendation for a transaction concerning one or more financial instruments, and this advice is not made more widely available to the public, is not an investment recommendation.

Media exception

The media are covered by an exception provision (Article 21 of MAR), on the basis of which, in terms of investment recommendations produced by others, regulation of investment recommendations does not apply, unless the recommendations are substantially changed in connection with media reporting. Moreover, journalists' own views, for example in connection with an article, fall outside the scope of application, provided that they are not made with the intention of deriving a financial advantage or distorting the market.

To whom does the regulation of investment recommendations apply?

'Information recommending or suggesting an investment strategy' means information produced by[1]

- an independent analyst

[1] *MAR 3.1 (34).*

- an investment firm
- a credit institution
- any other person whose main business is to produce investment recommendations
- or a natural person working for them under a contract of employment or otherwise.

The regulations also apply to other persons who repeatedly propose investment decisions in respect of financial instruments and present themselves as having financial expertise or experience or put forward their recommendations in such a way that other persons would reasonably believe they have financial expertise or experience (‘expert’).

When evaluating whether a person writing an investment column or blog, for example, can be considered to be an investment expert intended by regulation, attention should be paid to, among other things, the person’s previous work history and whether the person has professionally produced investment recommendations in the past, and whether their previous recommendations are or have been relayed by, for example, the media. Another important factor is how often a person produces recommendations and how the recommendations are distributed to an extensive group.

General obligations in relation to disclosure of interests and conflicts of interest

Articles 5 and 6 of the Commission Delegated Regulation provides for codes of practice in relation to disclosure of interests and conflicts of interest. This newsletter only addresses the essential aspects of disclosure of interests and conflicts of interest.

A producer of recommendations must disclose any relationship and circumstance that may reasonably be expected to impair the objectivity of the information. The objectivity of recommendations is considered to be impaired particularly when the producer of a recommendation has financial interests in the financial instrument that the recommendation concerns or significant conflicts of interest in respect of the issuer of the financial instrument. The producer of a recommendation must assess what kind of financial interests impair the objectivity of the recommendation or influence the investor’s decision-making. Factors impairing objectivity may be, for example, significant principle and secondary activities and holdings of the producer of an investment recommendation, or a family member, in the issuer that the investment recommendation concerns.

If the producer of a recommendation is a legal person, the above-mentioned requirement also applies to natural or legal persons who participated in producing the recommendation and who work for them under a contract of employment or otherwise.

If the producer of a recommendation is a natural person, the information to be disclosed should include any interests and conflicts of interest of persons closely associated with them in respect of the financial instrument or issuer that the recommendation concerns.

If the producer of the recommendation is a legal person, the information to be disclosed must also include any interests or conflicts of interest of any legal person belonging to the same group that are

- known, or reasonably expected to be known, to the persons involved in the production of the recommendation or
- known to persons who, although not involved in the production of the recommendation, have or could reasonably be expected to have access to the recommendation prior to its completion.

The FIN-FSA considers that information behind 'Chinese walls', for example, does not need to be presented in a recommendation, because such information is not expected to be available to the producers of the recommendation.

Additional obligations in relation to disclosure of interests and conflicts of interest

In addition, the Regulation[2] sets out a number of obligations in relation to the disclosure of interests and conflicts of interest for independent analysts, investment firms, other persons whose main business is to produce investment recommendations or a natural person working for them under a contract of employment or otherwise, and investment experts.

The above-mentioned persons must disclose the following information concerning the issuer to which the recommendation, directly or indirectly, relates

- a net long or short position exceeding the threshold of 0.5% of the total issued share capital of the issuer[3]
- if holdings exceeding 5% of the total issued share capital of the person producing the recommendation or any other person belonging to the same group with that person are held by the issuer, a statement to that effect.

The recommendation should also include a statement if the person producing the recommendation or any other person belonging to the same group with that person

- is a market maker or liquidity provider in the financial instruments of the issuer to which the recommendation relates
- has been lead manager or co-lead manager over the previous 12 months of any publicly disclosed offer of financial instruments of the issuer
- is party to an agreement with the issuer relating to the provision of investment services with the restrictions set out in Article 6 of the Delegated Regulation
- is party to an agreement with the issuer relating to the production of the recommendation.

In addition, the investment service provider must include a description of the effective internal organisational arrangements it has set up for the prevention and avoidance of conflicts of interest and the linkage to transactions in services of investment firms and trading fees of the remuneration of persons working for it and involved in producing recommendations.

How information is disclosed

Information on interests and conflicts of interest should, as a rule, be included in the recommendation itself. If this is unreasonable given the length or form of the recommendation, it is sufficient for the recommendation to indicate where the required information is available directly, easily and free of charge to the recipients of the recommendation.

In situations where the recommendation is not in writing and is presented, for example, through meetings, road shows or audio or video conferences as well as on radio, TV or websites the person who produces the recommendation should state in the recommendation where the required information in relation to interests and conflicts of interest can be accessed.

2 Article 6 of Delegated Regulation (958/2016).
3 See Article 3 of the 'Short-selling' Regulation (EU) No 236/2012.

If a given comment or statement merely repeats an investment recommendation published earlier by the same person and it does not include new assessments of the financial instrument or issuer, this does not constitute a new recommendation. The Regulation requires, however, that the date and time when the recommendation was first published be included in connection with the repetition.

For further information, please contact

Pia Ovaska, Legal Adviser, tel. +358 9 183 5296

Prospectus thresholds rise on 1 January 2019 − prospectus must be prepared for offers over EUR 8 million

Prospectus thresholds for the requirement for prospectus preparation and prospectus exemptions will rise when amendments to the Securities Market Act concerning prospectus thresholds enter into force on 1 January 2019. The EU Prospectus Regulation (1129/2017) and the amendments to the Securities Market Act will begin to be fully applied on 21 July 2019.

The general rule for the requirement to prepare a prospectus does not change: a prospectus is prepared when securities are offered to the public or admitted for trading on a regulated market, unless some prospectus exemption applies.

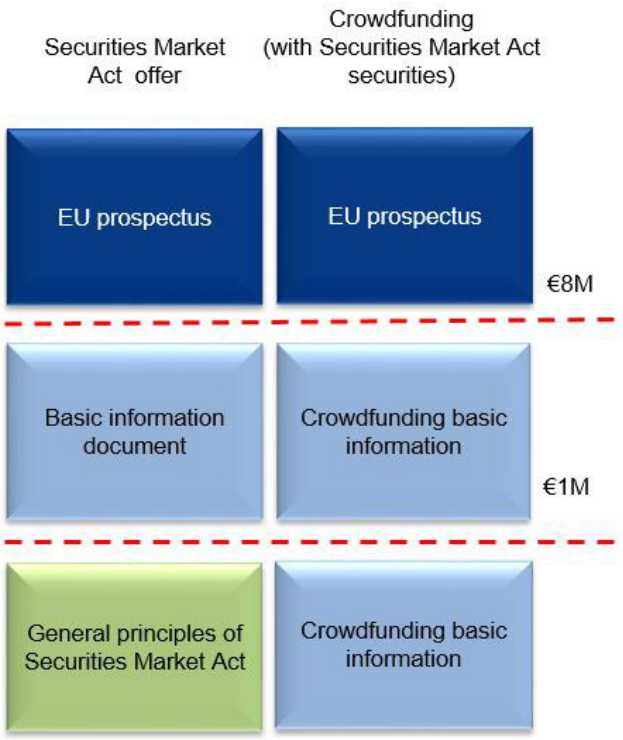
The requirement to prepare a prospectus does not apply to offers under EUR 1 million. The general principles of chapter 1 section 2–4 of the Securities Market Act do, however, apply to offers under EUR 1 million.

Changes as of 1 January 2019

- The current EUR 5 million EU prospectus threshold will rise to EUR 8 million (Member State option).
- The national prospectus will be discontinued. Currently, a national prospectus must be prepared for offerings of at least EUR 2.5 million and less than EUR 5 million.
- A basic information document must be published for securities offers of EUR 1–8 million.
  - The content requirements of the basic information document are laid down in a decree of the Ministry of Finance.
  - The basic information document is submitted to the FIN-FSA, but the FIN-FSA does not separately approve them.
- In the future, a First North company prospectus must include the information of the basic information document.

If securities are offered in crowdfunding, a crowdfunding basic information document in accordance with the Decree on Crowdfunding (1045/2016) should be prepared for all offers up to EUR 8 million.

Figure 1 Disclosure requirements in the offering of securities



For further information, please contact

Marianne Demecs, Market Supervisor, tel. +358 9 183 5366.

Events for listed companies 2018

In late November/early December, the FIN-FSA organised three events on listed companies' financial reporting, which attracted around 250 participants. Topics included new IFRS standards, better investor communications, IFRS enforcement observations and a review of other regulations relating to the disclosure obligations of listed companies. Professor **Esko Penttinen** of Aalto University and **Elina Koskentalo** of XBRL Finland participated in the event, addressing the topic of digitalisation of financial information.

The objective of events for listed companies is to gather together various stakeholders for financial reporting.

The presentation material (in Finnish) is available on the FIN-FSA website.

For further information, please contact

Supervision of Markets and Conduct of Business, tel. +358 9 183 5577.