

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. Articles other than those pertaining to IFRS enforcement will appear mainly in English. The newsletter is published by FIN-FSA's Market Supervision.

In this newsletter we will discuss the following topics:

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Topical matters at ESMA

Level 2 regulation relating to the Markets in Financial Instruments Directive and Regulation

ESMA has published a Discussion Paper on the Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR). It has also issued a request for comments on technical standards and advice on financial market structure and investor protection to the European Commission. ESMA requests comments by 1 August 2014.

Level 2 regulation relating to the Market Abuse Regulation

ESMA's Market Integrity Standing Committee is preparing a request for comments on level 2 regulation relating to the Market Abuse Regulation. A request for comments is planned to be published later in 2014.

ESMA has been mandated by the European Commission to prepare a technical standard relating to the Market Abuse Regulation and the reporting of infringements to competent authorities.

Level 2 regulation relating to the Central Securities Depositories Regulation

ESMA's Post Trading Standing Committee is preparing technical standards relating to the Central Securities Depositories Regulation. The commenting period on the Discussion Paper closed on 22 May 2014.

Technical standards relating to amendment of the Transparency Directive

The commenting period on ESMA's technical standard on notification obligations relating to amendment of the Transparency Directive closed on 30 May 2014. ESMA's Corporate Finance Standing Committee is currently analysing the comments received. ESMA is expected to deliver the draft technical standards to the European Commission in late 2014. Requests for comments on proposals relating to the European electronic access point to national central storage facilities and single electronic reporting format for listed companies (e.g. XBRL) are also expected in late 2014 or early 2015.

Prospectus Directive

ESMA's Corporate Finance Standing Committee is preparing technical standards relating to the Prospectus Directive regarding the approval and publication of prospectuses, the dissemination of advertisements, and information incorporated by reference. ESMA's obligation to prepare technical standards in these areas is regulated by the "Omnibus II" Directive. ESMA will be requesting comments on the proposals in late 2014.

Level 2 regulation relating to the Packaged Retail Investment and Insurance Products Regulation

The European Supervisory Authorities' Joint Committee's Sub-Committee on Consumer Protection and Financial Innovation has started preparing technical standards relating to the Packaged Retail Investment and Insurance Products (PRIIPS) Regulation. The related Discussion Paper is planned to be published in late 2014.

How FIN-FSA supervises disclosure obligations of listed companies and trading in the securities markets

The supervision of listed companies' compliance with the disclosure obligations and of trading on financial instruments falls within the area of responsibility of FIN-FSA's Market Supervision department.

In monitoring compliance with the disclosure obligation, FIN-FSA aims to ensure that listed companies provide information in accordance with the provisions of the Securities Markets Act (SMA). FIN-FSA also supervises listed companies' adherence to the International Financial Reporting Standards (IFRS) and the Accounting Act. The supervision focuses on listed companies' financial statements and interim reports and covers both the consolidated financial statements and the statutory financial statements. This article does not cover IFRS supervision.¹

Listed companies do not fall within the group of entities supervised by FIN-FSA; they are so-called other financial market participants. The supervision does not pertain to the listed companies themselves – but to information made public by them. Moreover, FIN-FSA's scope of responsibilities does not cover the application and supervision of general corporate law provisions.

The supervision of trading focuses primarily on suspected cases of market abuse, ie abuse of inside information and market manipulation.

Supervision of listed companies' disclosure obligations

The main objective of the supervision of compliance with the disclosure obligations referred to in the SMA is to ensure that investors have access to sufficient information on matters that are likely to have a material effect on the value of security. Monitoring is conducted both ex ante and ex post, including supervision visits, theme-specific reviews and investigations of identified irregularities relating to listed companies' disclosure obligations. FIN-FSA also provides listed companies with guidance on the code of conduct relating to the disclosure obligations.

¹ Link:http://www.finanssivalvonta.fi/en/Listed_companies/IFRS/Pages/Default.aspx.

As regards the ongoing disclosure obligation, FIN-FSA seeks to ensure that listed companies disclose, without undue delay, any such decisions and matters that are likely to have a material effect on the value of their securities. The supervision focuses eg on the clearness and justifiability of presented future prospects and the up-to-datedness of profit warnings.

With regards to disclosure of periodic information, FIN-FSA monitors the contents of financial reviews, which listed companies are obliged to publish on the basis of the SMA (interim report, interim management statement, annual financial statement and management report as well as financial statement release), to ensure that they comply with the legal provisions and that they are made public within the deadlines prescribed by law.

In this context, FIN-FSA focuses on ensuring that listed companies adhere to the provisions of the SMA, whereas NASDAQ OMX Helsinki (Helsinki Stock Exchange) monitors compliance with the rules of the Helsinki Exchange. The Finnish Corporate Governance Code is part of the Helsinki Exchange's rules, and this way the Helsinki Exchange monitors observance of the recommendations of the Code.

FIN-FSA's ex post supervision of listed companies' disclosure obligations is based on the Authority's own findings and observations from outside sources. On the basis of a supervisory finding, FIN-FSA may request a clarification from the company and, based on the company's reply, the Authority assesses whether further supervisory measures are needed (see 'Supervisory measures and publication of information' below).

Supervision of trading

The functioning of securities markets requires that investors have confidence in the markets and the parties operating in them. Market abuse erodes this confidence. In supervising trading, FIN-FSA seeks to prevent inappropriate behaviour in the markets and investigates suspected cases of market abuse.

The stock exchange is responsible for overseeing real-time trading and trading participants' compliance with the rules of the trading venue.

Inspection of insider trading

The aim of insider investigation is to find out whether inside information has been abused in securities trading. An inspection generally begins with the disclosure of material information having an effect on the price of security. Such information refers, for example, to significant corporate restructurings, agreements or profit warnings, in connection with which trading is investigated routinely. FIN-FSA may also receive notifications of suspicious transactions from brokers and the stock exchange. A more thorough investigation is commenced if the price development of a company's share has changed exceptionally or the share trading volume has clearly increased for example, such as prior to the publication of an announcement.

In an actual investigation, FIN-FSA examines securities trading volumes and price development over a longer period. FIN-FSA requests the listed company, whose share or other financial instrument trading is being investigated, to submit information on all the persons involved in the matter for example in a corporate acquisition (project-specific insider register) and on the point in time when such insiders have become aware of the matter. The company is also requested to give a chronological description of the project investigated. FIN-FSA may also request such descriptions from all parties involved in the project, such as the issuer's economic or legal advisers. In addition to persons who have gained insider information, FIN-FSA investigates trades of parties closely associated with the insiders, corporations controlled by the insiders and corporations in which the insiders exercise influence. Trades of foreign parties are also investigated, and the related information is requested from the respective foreign supervisory authority.

Market manipulation

Market manipulation means any inappropriate action taken with the intention to artificially affect – directly or indirectly – the demand, supply or the price of a financial instrument. Market manipulation can occur either by taking misleading actions or by providing false or misleading information about a financial instrument.

Market manipulation investigation mostly commences if trading includes features that do not appear to be in line

with usual trading practices. In investigating such cases, FIN-FSA uses information submitted to the Authority in transaction reports and data obtained from the stock exchange's trading system.

Supervisory tools

Trade reporting

In supervising trading, FIN-FSA uses information on transactions in financial instruments submitted to the Authority by investment service providers. The reporting obligation is based on the Markets in Financial Instruments Directive (MiFID) and gives a better picture of executed trades, enables supervision of off-exchange trading and information exchange between European supervisors. FIN-FSA's framework for trade reporting is part of the European data collection and data exchange framework for transactions in securities.

Investment service providers' obligation to notify suspicious transactions

FIN-FSA investigates suspected market abuse on its own initiative, but it also receives information on suspicious cases through notifications, tip-offs and declarations eg from the stock exchange, market participants, the media, individual investors and foreign supervisory authorities.

Finnish investment service providers and Finnish branches of foreign investment service providers are obliged to notify FIN-FSA without undue delay if they have reason to suspect that a transaction may involve the use of inside information or market manipulation. The notification obligation also pertains to persons employed by investment service providers. The notification obligation is personal, and violation of the obligation may lead to a penalty payment prescribed by law.

A notification relating to market abuse is not an investigation request in nature. Rather, it is the observation of an atypical transaction or fact by the party submitting the notification; where there might be reason to suspect that the transaction may involve illegal use of inside information or market manipulation.

In its supervision, FIN-FSA has emphasised that notifications of investment service providers and other parties regarding suspicious transactions are very important in ensuring efficient supervision and reliability of the markets.

Supervisory measures and publication of information

As a supervisory measure, FIN-FSA commences a so-called administrative hearing if it considers that a suspected case involves neglect or violation of the provisions of the SMA. An administrative hearing may lead to an administrative sanction (administrative fine, public warning or penalty payment). The fact that FIN-FSA has imposed an administrative sanction is public information. If there is reason to suspect that an act fulfils the constituent elements of an offence under the Penal Code relating to disclosure obligations in the securities markets, illegal use of inside information or market manipulation, FIN-FSA will request a police investigation. Such a request is secret until the case has been heard in a court of law or has been dismissed.

As a rule, information regarding supervisory measures directed at individual actors is not made public. Information concerning possible reviews or supervisory measures relating to individual financial market participants is to be kept secret by virtue of section 24, subsection 1, paragraph 15 of the Act on the Openness of Government Activities (Openness Act),² if access to the information would compromise the inspection or the achievement of its objectives. Requests for clarification, the related responses and FIN-FSA's supervisory letters are typically such in nature that they are confidential on the basis of the Openness Act.

Twice a year, FIN-FSA publishes statistics on investigated cases of suspected abuse in the securities markets, administrative sanctions imposed and requests for police investigation. The statistics are available on the FIN-FSA website.³

The number of investigated cases varies annually. Suspected cases of market manipulation typically increase when share prices fluctuate markedly. In the same vein, insider investigations generally increase when economic activity picks up or there are more corporate restructurings or profit warnings, and decrease when the opposite is the case.

2 Openness Act, section 24, subsection 1, paragraph 15: "... the following official documents shall be secret: ... documents containing information on inspections or other supervisory tasks of the authorities, if access would compromise the inspection or the achievement of its objectives, or without a pressing reason cause injury or suffering to a party".

3 Link: <http://www.finanssivalvonta.fi/en/Statistics/sanctions/Pages/Default.aspx>.



Supervisory findings on profit forecasts

As part of the supervision of listed companies' disclosure obligation, FIN-FSA monitors the assessments of future prospects provided by listed companies. In this supervision, attention is paid, among other things, to the qualitative characteristics of profit forecasts, such as clarity, unambiguity, consistency of terminology as well as the justifications provided for the profit forecast and the degree to which it is achieved. Furthermore, the timing of profit warnings issued is monitored.

Profit forecast

According to chapter 3, section 1, subsection 6 of the Accounting Act, a listed company shall present an assessment of expected future performance in its management report. The company may choose whether to present this assessment as a general statement on the future outlook or as a profit forecast. The company may also present its prospects in its interim report and financial statement release.

In FIN-FSA regulations and guidelines,¹ profit forecasts refer to the issuers' projections for future periods, whose wording directly or indirectly indicates the likely minimum or maximum level of the issuer's future profit or loss. Profit forecasts may also be information that enables calculation of an approximate sum of future profits or losses. Profit forecasts include as an example assessments of changes in profitability, the level of operating profits, the profit or loss for the financial period, or the operating profit or loss margin. Profit forecasts may take the form of either numerical or verbal representation.²

By a so-called loose profit forecast, FIN-FSA refers to a forecast which does not explicitly indicate the extent of change in the result, for example *"operating profit is expected to increase"* or *"operating result is expected to be negative"*.

Presentation of profit forecasts

Profit forecasts should be presented consistently. Profit forecasts should also be as unambiguous and clear as possible. They should clearly indicate the key figure concerned (operating profit, pre-tax profit, EPS), the period assessed (full year, present quarter) and the comparative

period (previous year, corresponding quarter of the previous year, preceding quarter of the present year). Usage of the term "result" alone is not recommendable, since one cannot unequivocally interpret the result being assessed. For example, the profit forecast *"The result for 2013 is expected to significantly exceed the previous year's level"* does not indicate, whether it is the operating profit, profit before taxes or profit for the period that is concerned.

The wordings indicating the extent of change in profit forecasts should be consistent. FIN-FSA recommends that listed companies define internally, to the extent possible, what the terms used in the profit forecast (eg improves, improves somewhat) mean in euro or percentage terms. For example, the wording "improves somewhat" should as a rule refer to a change of the same magnitude from a financial period to another if there are no significant changes in the operations or in the operating environment.

Consistency in the presentation of a profit forecast also means that the key figure for which the profit forecast is initially provided should not be replaced during a financial period without proper justification. If the key figure is replaced, the achievement of the forecast for the replaced key figure should also be addressed in this context.

As an example, a company provides the following profit forecast in its financial statement release *"the result is expected to be better than in the previous year"*. In its Q1 interim report, it provides a forecast for the operating profit (*"better than in the previous year"*) and the profit for the period (*"significantly better than in the previous year"*). According to the company's internal forecast, the profit forecast provided for the operating profit no longer appears to be achieved due to higher-than-expected expenses accrued in Q2. In its Q2 interim report, the company lowers the profit forecast concerning the profit for the period (*"significantly better"* -> *"better"*) and omits the forecast for the operating profit by not commenting on it at all. A weakening of the forecast for the operating profit can certainly be interpreted, since the forecast concerning the profit for the period has been lowered. Later during the period, the company accrues expenses that it determines as non-recurring.

However, the stock exchange release disclosing these non-recurring expenses does not address how these expenses affect the forecast concerning the profit for the period but

¹ FIN-FSA regulations and guidelines 7/2013, chapter 7.8, paragraph (63).
² FIN-FSA regulations and guidelines 7/2013, chapter 7.8, paragraph (65).



only comments on the development of operating profit before extraordinary items. However, also in this context, the impact of non-recurring expenses on the profit forecast concerning the profit for the period can be deduced. During the rest of the period, the company only comments on the development of the operating profit, excluding non-recurring items.

In the example above, instead of the practices described, it would be recommendable that the company had provided, at the beginning of the period, a profit forecast/forecasts clearly indicating the key figures whose performance is forecasted, and continued to comment on the achievement of profit forecasts from these key figures consistently in each financial report and release during the period as well as the impact of any non-recurring items on them.

Future prospects provided for 2013

The future prospects for 2013 reviewed by FIN-FSA (covering 121 listed companies) were divided as follows:

- 9 companies: general statement on the future outlook
- 3 companies: revenue forecast
- 20 companies: profit forecast
- 87 companies: revenue and profit forecast
- 2 companies: no assessment of prospects (justifications provided).

As regards the profit forecasts (total of 112)³, almost all had been provided for the operating profit: 45 forecasts were provided on reported operating profit or operating profit margin and 35 forecasts were provided on adjusted operating profit or margin (adjusted for non-recurring items or otherwise). Nine profit forecasts were provided for EBITDA or EBITDA margin. There were also 23 profit forecasts for other results than those referred to above, five of which did not indicate the type of result concerned. A majority of the profit forecasts provided by the companies consisted of loose profit forecasts.

The period covered by the forecast was clearly indicated in all profit forecasts. Almost all of the profit forecasts were provided for the full year. Five companies had provided a profit forecast for the present quarter. A few companies had

provided a profit forecast for both a shorter period than a year and the full year.

A few companies had also provided a general future outlook at the beginning of the financial period or shortened the period covered by the outlook, deviating from their previous practice. The change of the manner of presentation was justified, and later during the period the presentation of outlook for the full period was resumed, which FIN-FSA considers good practice.

In general, FIN-FSA considers the manner of presentation of future outlook by listed companies good and clear; the companies had, almost without exception, defined which result was assessed in the profit forecast, and had also defined the period covered by the forecast clearly.

Realistic and achievable profit forecast

Companies' internal budgeting and forecasting cultures may differ materially; some companies may prepare a budget used as the basis for their internal incentive programme and its achievement may be very challenging. Some companies may prepare a very conservative budget, in addition to which they provide various scenarios prepared by the management. Although the profit forecast should be based on the company's internal assessment of its performance in the present financial period, the disclosed profit forecast does not have to be the same as its internal budget or forecast. FIN-FSA recommends that companies document the assessments used internally as the basis of the profit forecast, and if deviations are made from the internal budget/forecast, this should also be documented. Attention should be paid to ensuring that the disclosed profit forecast is realistic and achievable. The profit forecast may not be overly optimistic – it does not suffice that the achievement of the forecasted result is possible, but it should be likely.

Assessment of the issuance of a profit warning in the context of a loose profit forecast

According to chapter 6, section 4 of the SMA, a profit warning shall be issued without undue delay if it is likely that the financial performance differs materially from previously disclosed future prospects.

Especially in connection with a loose profit forecast, FIN-FSA recommends that the company, to the extent possible,

³ All profit forecasts; some companies had provided a profit forecast for several key figures.



defines internally an allowed range for the forecast (the so called profit of pipeline). The purpose of the pipeline is to support and facilitate the company's internal assessment of the need for issuing a profit warning. In accordance with FIN-FSA's view, the determination of a pipeline promotes consistency in issuing profit warnings. There are many possible ways to determine a pipeline. For example, for margin levels close to zero, the range may be determined in euro terms even if the range was otherwise defined in percentage terms.

As a rule, the allowed range of the profit forecast can not be considered to be anything between zero and the company's internal forecast for operating profit.⁴ For example; the profit forecast "*the operating profit is expected to be positive*" does not indicate the level of operating profit assessed by the company. If the company's internal budget/forecast used as the basis for the disclosed forecast weakens materially, even if it remains in line with the loose profit forecast by being "*positive*", the company should assess the need for issuing a profit warning already before the "*positive*" turns into "*negative*". In the context of a loose forecast, market participants use, among other things, the company's actual operating profits for the previous years in making their assessment for the level of operating profit for the present year. If it is likely that the development of the company's internal forecast for operating profit differs from the investors' justified expectations, the company shall, in accordance with FIN-FSA's interpretation, assess the need for issuing a profit warning under chapter 6, section 4 of the SMA. This assessment should always be based on the investors need for information in order to be able to make an informed assessment. If the issuer determines that information on the differences is likely to have a material effect on the value of the issuer's security, in accordance with FIN-FSA's interpretation, the obligation to issue a profit warning under chapter 6, section 4 of the SMA arises on the issuer.⁵

⁴ See also Helsinki Court of Appeal 31 October 2008 J No 07/550: The Court considered that the wording "under 10%" could not, in light of the company's previous disclosures, refer to any figure between zero and 10%; instead, it gave the impression of the operating profit being few percentage points below 10% at the maximum. The company should have, considering the requirement of timely disclosure, corrected its previous forecast based on its internal profit forecast already ahead of the Q3 interim report.

⁵ FIN-FSA regulations and guidelines 7/2013, chapter 5.6, paragraph (44).

Disclosure of annual financial statements and management report

FIN-FSA draws the companies' attention to the following aspects in the disclosure of annual financial statements and management report.

Disclosure procedures relating to annual financial statements and management report

FIN-FSA's Regulations and guidelines 7/2013 on disclosure obligation on issuers provides guidance on the disclosure procedures for regulated information. Under section 11.2.1, paragraph (7) of the regulation, in the disclosure of periodic reports it is enough to issue a release to the media containing such information from these reports as is likely to have a material effect on the value of the security, together with a notice that the report has been disclosed. The release shall also indicate where the report is made available to investors. The release that is filed with the operator of the relevant regulated market and the OAM shall be accompanied by a periodic disclosure report in full.

According to FIN-FSA's findings, the required appendices have been missing particularly from stock market releases on the disclosure of annual financial statements and management report. Such shortcomings have not, as a rule, been observed in the stock market releases on interim reports.

A stock market release on the disclosure of annual financial statements and management report must have the following appendices:

- complete annual financial statements, i.e the annual financial statements of the parent company as referred to in the Accounting Act, including the consolidated financial statements
- management report
- corporate governance statement, if it is issued as a separate report
- audit report.

The above-mentioned documents may also be disclosed as part of the annual report, provided that the documents are included, in full.

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In the disclosure of annual financial statements and management report it is therefore not enough to make the documents available on the issuer's website, but information on the disclosure must be communicated in a stock market release, to which the above-mentioned documents must be appended.

Time limit for disclosure

FIN-FSA also draws companies' attention to the fact that under chapter 7, section 5 of the Securities Markets Act, the issuer shall disclose its annual financial statements and the management report without undue delay, but no later than three weeks prior to the General Meeting of the Shareholders where the annual financial statements are to be presented for adoption, however, no later than three months after the termination of the financial period.

For further information, please contact:

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