SwissBanking

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Directives on the Independence of Financial Research

Content

Introduction

The following Directives have been issued by the Board of Directors of the Swiss Bankers Association (SBA) with a view to ensuring the independence of financial research. One of the purposes of the Directives is to avoid or limit any potential conflicts of interest associated with the preparation of financial research reports, or at least to require proper disclosure. In addition they aim generally to create appropriate transparency and ensure the equal treatment of all recipients of financial research. Clients who make their investment decisions based in part on recommendations made by financial analysts should be able to rely upon these analysts having conducted their research objectively, in good faith and with due diligence.

The ultimate objective of these Directives is to maintain and enhance the reputation of the financial research provided by the Swiss financial services industry, and the reputation of the Swiss financial centre as a whole, by sustaining and strengthening investor confidence in the efficient operation of the Swiss capital market.

The purpose of the Directives is not to prescribe standard internal structures and procedures within banks. They are free to structure and implement these Directives as they see fit, provided that they meet the minimum requirements set out in the Directives.

The Directives are to be considered as a code of conduct. They have at least no direct effect on the legal relationship between banks and their clients. Any such relationships are based on legal provisions and any particular contractual agreements made between banks and their clients.

1. General provisions

1 Financial analysts within the meaning of these Directives means employees of banks or securities traders (hereinafter referred to as "banks") who are engaged in compiling and producing the bank's research reports (in particular investment and financial recommendations) which are destined for external publication. Socalled "buy-side" analysts and "sell-side" analysts, in particular, fall within the scope of application of these Directives. The Directives apply to analysts who conduct primary and secondary research. Furthermore, they apply to both equities and fixed-income analysts. A financial analyst may not circumvent the provisions contained in these Directives by conducting transactions through third parties, such as members of his / her family or other persons close to him / her.

2 Investment and financial recommendations for bankinternal purposes only (such as portfolio and risk management, proprietary trading) that are not provided to clients or made accessible to a broader public (e.g. through publication on intranet or internet sites) do not fall within the scope of application of these Directives. In these Directives, any information which contains target prices for securities is also classified as a recommendation. The Directives also apply to in-depth interviews of and statements by financial analysts in the print media.

3 The Directives apply to banks domiciled in Switzerland. Banks may not use any of their branches abroad and group companies operating abroad in the banking and financial sector to circumvent these Directives.

4 These Directives allow all banks the right to produce financial research, or have research produced, on any company. In this regard, however, the following principles must be observed. If, despite compliance with these Directives, a conflict of interest for the bank's financial research activities cannot be avoided in an individual instance, or cannot be satisfactorily resolved, the bank must forgo publication of research reports on the company in question.

Commentary

The treatment of technical analysis (chart analysis) and pure “recommendation lists” etc. is set out in Circular 7258 of 15 May 2003.

Pursuant to principle 2, the Directives also apply to statements “of a research-like nature” in the print media by financial analysts. A statement is deemed to be “of a research-like nature” if it can be assumed that it will be perceived by the public as research (or the result of research).

In connection with principle 3 in particular, please refer to the more precise definition of the general scope of application given in Circular 7410 of 3 June 2005.

2. Principles for internal organisation

2.1 Relationship with new issues department and investment banking

5 The organisational unit responsible for financial research (hereinafter referred to as "financial research") must be independent, from an organisational, hierarchical, functional and locational perspective, from the unit that is responsible for issuing securities and for investment banking.

6 The remuneration paid to financial analysts must not be dependent upon the performance (revenues or performance target) of one or more specific transaction(s) of the new issues department or investment banking.

7 If the remuneration paid to the financial analysts is based generally upon the performance of the new issues department or investment banking, this must be disclosed in reports and recommendations.

8 The new issues department and investment banking operations of a bank and its financial research unit must be structured in such a manner that basically no privileged information ("material, non-public" information) flows between them that is not simultaneously available to clients of the bank (Chinese walls). Prior approval by the unit of the bank responsible for compliance (hereinafter referred to as the "Compliance Unit") is required for any exceptional cases where such information is exchanged despite this requirement. This unit must ensure, in particular, that the exchange of information occurs within the framework of a regulated process. The negative consequences of conflicts of interest must be avoided in such a process.

Commentary
Financial analysts of a bank who are also frequently involved in the pricing of an issue must not be disposed to give a more favourable opinion of a company than they would normally do of their own accord. It must also be ensured that financial analysts and other persons who are directly involved in the preparation of an issue and as such, have access to information ("material, non-public" information) relevant to pricing that has not (yet) been made public, do not gain any benefit from same.

9 Any front-running in securities due to be issued by analysts or other employees of a bank who might benefit from the issuance of a security, is prohibited.

Commentary
This guideline is intended to prevent front-running, particularly by analysts. Nevertheless, analysts, like all other investors, may subscribe for new securities of a particular issue.

10 Research reports may not be sent to the investment banking department prior to their publication either for approval or for complete perusal. A financial analyst may only contact the investment banking department, orally or in writing, for the purpose of checking facts. Any such communication must be carried out with the involvement of the Compliance Unit, or in accordance with a process approved by same, and must be recorded in writing.

11 Financial analysts must not be disposed to write research reports with a predefined conclusion, but must rather, in all cases, be able to reach an independent opinion.

12 In any published research reports, the bank must disclose whether it has participated in the last 12 months in any issue of securities on behalf of the company being researched.

Commentary
Disclosure with respect to any relationship with an issuer needs only to include facts that are considered public under the bank's mandate in respect of the issue. If the facts are not public, any disclosure may only be made with the express consent of the issuer (Banking Act, Art. 47). Consulting mandates are also deemed to be a participation in an issue of securities.

2.2 Relationship with securities trading (including proprietary trading) and sales

13 Financial analysis must be independent, from an organisational, hierarchical and functional perspective, from any units that are responsible for securities trading (including proprietary trading) and sales.

14 The remuneration paid to financial analysts may not be dependent upon the performance (revenues or performance target) of one or more specific securities trading (including proprietary trading) or sales transaction(s).

15 If the remuneration paid to financial analysts is based generally upon securities trading performance (including proprietary trading) or sales, this must be disclosed in reports and recommendations.

Commentary

Financial analysts should not be permitted to make unfounded buy and sell recommendations in the interests of securities trading or sales. Proprietary trading units may also not optimize their positions with the improper assistance of analysts. An example of such improper conduct shall be if securities are bought by the proprietary trading unit on the recommendation of analysts before bank clients are informed about the recommendation in question (see para. 24).

The separation discribed in para. 13 must also be locational in respect of the relationship between financial analysis and securities trading (including proprietary trading). In contrast, the separation between financial analysis and sales does not necessarily require separate premises.

Asset managers and corresponding organisational units of banks that conduct only buy-side research, are exempt from para. 13. Where securities executions alone are handled within the same organisational unit that also prepares research reports (e.g. an order routing or execution desk within the portfolio management unit), compliance with para. 13 may be waived.

Companies that operate exclusively as brokerage companies (including research) are exempt from para. 13 if it can be ensured by some other means that the securities sales do not influence the research activities.

16 Securities trading (including proprietary trading) and financial research of a bank must be structured in such a manner that basically no privileged information ("material, nonpublic" information) flows between them that is not simultaneously available to clients of the bank (Chinese walls). For the exceptional case that such information is exchanged despite this, the Compliance Unit of the bank is required to be involved. This unit must ensure, in particular, that the exchange of information occurs within the framework of a regulated process. The negative consequences of conflicts of interest must be avoided in such a process.

Commentary
The transmission by financial analysts of information to the securities trading and sales department of a bank about any changes to recommendations that may have been decided is permitted, provided it is ensured that the employees involved in these departments do not use this information for front-running operations for the benefit of their own positions or those of the bank (nostro). The corresponding measures are to be appropriately documented.

2.3 Relationship with credit department

17 Financial analysis must be independent, from an organisational, hierarchical, functional and locational perspective, from any units responsible for lending business.

18 The organisational unit responsible for lending to corporate clients and the financial research unit must be structured in such a manner that basically no privileged information ("material, non-public" information) flows between them that is not simultaneously available to clients of the bank (Chinese walls). For the exceptional case where such information is exchanged despite this, the Compliance Unit of the bank is required to be involved. This unit must ensure, in particular, that any exchange of information occurs within the framework of a regulated process. The negative consequences of conflicts of interest must be avoided in such a process.

19 Any information obtained by advisors of corporate clients that is classified as confidential may not be passed on to financial research of the bank.

Commentary
In the interests of the bank and its clients, loan officers responsible for lending to corporate clients and financial analysts exchange client information. However, financial analysts should not have any incentive to protect their banks' loan portfolios for short periods by making unfounded positive recommendations. In addition, if a client's loan position deteriorates, the loan officers responsible may not advise financial research and proprietary trading in advance. Measures must therefore be taken to ensure the independence of financial analysts in such situations as well. The above principles govern this exchange of information.

2.4 Equity participations held by a Bank

20 If a bank holds more than 50 percent of the voting rights of a listed company, the bank may not include any such companies in any of its own financial research (no reports, no recommendations).

21 If a bank holds a percentage of voting rights equal to or greater than the threshold values with regard to the disclosure of shareholdings (notification duty set out in FMIA / FMIO-FINMA), any financial research contained in reports or recommendations relating to any such company must disclose the relevant threshold value in terms of the situation shortly prior to publication of the report or recommendation. In case of companies that do not have their primary listing on Swiss exchange, equivalent foreign provisions may be used in connection with the threshold values and to assist in the calculation of percentage voting rights.

22 Any other potential conflicts of interest must be disclosed in any publication of research reports, unless the bank chooses not to prepare such reports.

23 Proprietary securities (including derivatives), and those of companies that belong to the same group, are not to be included by banks in published recommendations or reports.

Commentary
As a rule, the banks' equity participations in listed companies are not held for short-term investment purposes. Significant participations are also usually disclosed. Nevertheless, there is the risk of a conflict of interest when analysts give an opinion on listed companies in which their employers own an interest. In order to avoid this risk, restrictions apply on a graduated scale to financial research where there is a significant participation in the company concerned. Percentages that have already been calculated elsewhere (e.g. percentage voting rights as at the end of any previous month) may also be used to disclose voting rights pursuant to para. 21. Otherwise, percentage voting rights must be disclosed as of a date 10 days prior to publication of the report or recommendation.

3. Principles for external relationships

3.1 Relationship with bank clients

24 As a rule, reports and recommendations by financial analysts, particularly any ratings that are published or changed, are to be made available to all recipients in a client category (recipient group) within and outside the bank at the same time. Internal and external parties and offices may only be given advance notice in exceptional cases and in accordance with the Directives of the Compliance Unit.

Commentary

Financial analysts provide information to both bank clients and bank departments. Analysts may not discriminate in their treatment of the various addressees in a client category (e.g. by fax, by e-mail, by internet, etc.). In particular, they may not give preference to selected (potential) clients within a recipient group by providing information that other clients in the same recipient group do not simultaneously receive and in such a way that the addressees given preference might be able to derive an advantage in the stock market from it. This also applies to proprietary trading by banks (see para. 13–16).

Equal treatment from a temporal point of view means distributing information in a manner that ensures the information is (potentially) available to all addressees in a recipient group at the same time. In particular, equal treatment in temporal terms means posting the information on the bank's internet site and mailing the information in electronic form (e-mail) at the same time.

If advance information is provided by way of exception, the Compliance Unit must be notified in advance of the group of recipients to receive this information. The bank issues regulations in this regard, defining how and under what conditions information may be passed on in advance. One possible solution is to adequately brief any persons or units provided with information in advance about the confidential nature of the information, and have them sign a confidentiality agreement to be provided to the Compliance Unit. In such an agreement, they undertake to refrain from passing on to third parties any such information received before it is made generally public, and refrain from using it for investment decisions.

3.2 Relationship with companies being analysed

25 As a rule, a company shall not disclose to individual analysts any kind of privileged ("material, non-public") information. If an analyst nevertheless does receive privileged information in the course of his/her activity, he/she shall decide in consultation with the Compliance unit on how to proceed, in particular, on whether to refrain from publishing the report or recommendation, as well as on whether to disclose that the information could have been privileged.

26 Any bank that is involved in an initial public offering (IPO) as a manager or comanager may not publish any new reports on the company in question or provide any new recommendation for a period of 40 calendar days following the first day of trading ("quiet period"). By way of exception, the period of 40 calendar days may be shortened with the consent of the Compliance Unit.

27 Any bank that is involved in a secondary public offering (SPO) as a manager or comanager may not publish any new reports on the company in question or provide any new recommendation for a period of 10 calendar days following the date on which the shares were allocated ("quiet period"). By way of exception, the period of 10 calendar days may be shortened with the consent of the Compliance Unit.

Commentary
If, within a bank or bank group, the organisational unit that is involved in an IPO or SPO as manager or comanager is separate from other parts of the bank or group from an organisational and hierarchical perspective, so that no privileged (“material, non-public”) information is able to flow, paras. 26 and 27 will not apply for organisational units that conduct purely buyside research.
Approval to shorten the 40 or 10-day deadline may be given, by way of exception, if there is some significant news or a significant event relating to the company in question to be passed on in the interests of investors.

28 A financial analyst may not provide the company with any research results for approval before those results have been published. Any perusal of information by the company to be evaluated prior to publication of the results may only be for the purpose of checking facts.

Commentary
The company may not be notified of the investment summary or target price in advance. A complete draft of the research report must be provided to the Compliance Unit before the company may be provided with facts from the research report. In the event that a financial analyst wishes to subsequently change the research rating or target price, he must provide written reasons for this, document the change, and obtain approval from the Compliance Unit for any such change.

29 A financial analyst may notify the company to be evaluated about any rating change one day prior to publication of the research report, but only after the close of trading on the stock exchange(s) where the company in question is listed.

Commentary

The purpose behind the prohibition against disclosing a rating change to the analysed company before the close of trading is to avoid the financial analyst being influenced by the analysed company, and to avoid any front-running by representatives of the analysed company.

30 A financial analyst may not give any promises that favourable research reports, a specific rating or a specific target price will be published.

31 Analysts may not accept any privileges, gifts or any other favours from the company being analysed where the value of such privileges, gifts or favours excedes that of normal occasional gifts. If there is any doubt, the analyst must notify the Compliance Unit about any offers received. The bank will set out the procedure to be followed in any such case in an internal directive.

Commentary

Banks must counteract any potential risk of attempts to influence financial analysts, by issuing, among other measures, directives governing permitted gifts, privileges and other favours as well as the relevant corresponding courses of action. In addition, any costs that are directly or indirectly related to a research report, such as the costs of travel and accommodation for financial analysts, are to be paid in all cases by the employer of the analyst, i.e. by the bank.

3.3 Proprietary trading by financial analysts

32 A financial analyst may not acquire for his / her own account any securities which he / she researches (securities, uncertificated securities, incl. derivatives).

Commentary
This principle is applicable to all research reports for which the financial analyst is responsible or in the preparation of which he / she played a key part, and which are intended for publication. This principle shall apply irrespective of whether the analyst works as a buy-side or sell-side analyst. The following rule governs circumstances prevailing at the time these directives come into force: as stated in para. 32, a financial analyst may not acquire for his / her own account any securities which he / she researches. Should the analyst wish to continue to hold securities al-ready in his / her possession, then he / she must declare in the research report about the relevant company that he / she owns securities in this company (but without revealing the quantity or value). Any sale of securities in companies which the financial analyst has researched is only possible with the consent of the Compliance Unit. These regulations for "buy", "hold" and "sell" also apply in cases where a financial analyst is newly employed in a bank, or is given new research tasks by his / her employer. Details are set out in Circular 7258 of 15 May 2003.

33 If an analyst holds an executive function, or has any other significant influence in the company to be researched, he / she may not prepare any research reports on the company.

4. Concluding provisions

34 Banks must publish the basic methodology used for their financial research in a generally accessible and regularly updated form. They must take care when formulating their investment and financial recommendations and their ratings to use clear and understandable language.

35 Banks must issue the necessary directives and implement appropriate organisational measures to ensure that these Directives are complied with at all times and monitored on an ongoing basis.

36 Internal audit must review compliance with the Directives on a periodic basis.

Commentary
In connection with para. 34, documenting the basic methodology used for analysis in the annual report shall be deemed to be an appropriate form of publication. Furthermore, banks may also make the corresponding information available by posting it on electronic media (internet). A separate publication on the methodology used for financial research is not required.
These Directives were adopted by resolution of the Board of Directors of the Swiss Bankers Association (SBA) on December 2, 2002 and were ratified on January 23, 2003 by resolution of the Swiss Federal Banking Commission (SFBC) as representing a code of conduct. They entered into effect on July 1, 2003. The present revised version has been approved by the Swiss Financial Market Supervisory Authority (FINMA) and enters into effect from February 1, 2018.

5. Glossary

A "buy-side analyst" is a financial analyst who prepares research reports for portfolio managers, fund managers, relationship managers or for private banking (or clients of private banking).

A "Compliance Unit" is an office within a bank that is responsible for compliance. It can be either an organisational unit that specialises in compliance or an organisational unit that performs tasks relating to compliance, amongst other things. In both cases, this organisational unit may consist of one employee only.

Financial Research is the organisational unit of the bank responsible for the financial research function. The term "financial research" may, among other things, stand for the corresponding activity or function, the responsible organisational unit or even the corresponding product of this activity. In these Directives, the term is used in the sense of organisational unit.

A "financial analyst" is an employee of a bank or a person commissioned by it who is engaged in compiling and producing a bank's research reports (in particular investment and financial recommendations) which are destined for external publication. This definition applies irrespective of whether the person holds the title of financial analyst or not.

Company is any juristic person which is the subject of research reports or recommendations that will be published.

Material, non-public information is information about a company that is not available to market participants and the disclosure of which would significantly influence the share price of the company, or would cause an average investor to expect such an influence.

Primary research includes financial research activities that are based on direct contact with the management of the company being researched as well as the subsequent analysis based on company data.

Research report is any written or electronic communication that a bank has distributed or will distribute to its clients or the general public which, as a product of its financial research activities, reflects an opinion or recommendation about a company or a security. In particular, reports, analyses and recommendations (including information on target prices and rating changes) are deemed to be research reports.

Secondary research includes financial research activities that are based on information available to the general public and opinions from experts (including analysts who conduct primary research).

Sell-side analyst is a financial analyst who prepares research reports on companies within a securities firm or the investment banking department of a bank. These research reports are intended for securities traders or professional market participants.

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