

December 20, 2022

## Imposition of Disciplinary Actions against SMBC Nikko Securities Inc.

Tokyo Stock Exchange, Inc. (TSE) has taken the following disciplinary action against SMBC Nikko Securities Inc. (hereinafter, “the Company”) in accordance with Article 34, Paragraph 2 of the Trading Participant Regulations and has requested the Company submit a business improvement report pursuant to Article 19, Paragraph 1 of the same Regulations.

### 1. Content of Disciplinary Action

- Suspension of securities trading on the Tokyo Stock Exchange for the proprietary account of the Equity Department (excluding activity specifically authorized by TSE, such as transactions associated with the fulfilment of contracts already existing before the announcement date of disciplinary actions) during the period from January 16, 2023 through January 20, 2023.
- Imposition of a fine in the amount of JPY 300 million

Note: The decision on this case was made based on the outcome of deliberations carried out by Japan Exchange Regulation.

### 2. Reasons

- (1) Conduct of making illegal purchases, etc. for the purpose of stabilizing market prices of listed shares

With regard to ten issues of listed shares, the Company attempted to prevent their closing prices on the execution dates of "block offer" trading, which served as the basis for the trading prices in the block offers, from significantly declining from their closing prices on the immediately preceding dates, thereby maintaining their share prices at certain levels. To that end, in violation of the provisions of Article 20 of the Order for Enforcement of the Financial Instruments and Exchange Act, the Company made purchases and offers to purchase at a series of limit prices for the purpose of stabilizing

(Reference Translation)

the market prices of the respective shares (hereinafter referred to as the "conduct in this case").

The conduct in this case is found to be in violation of Article 159, paragraph 3 of the Financial Instruments and Exchange Act (hereinafter referred to as the "FIEA").

In addition, the conduct in this case is found to have been committed due to insufficiency in the Company's control environment for transaction screening aimed at checking and preventing unfair transactions and in its control environment for governance aimed at ensuring strict legal compliance and appropriate business operations.

## (2) Deficiency in the control environment for transaction screening

The Company conducts transaction screening for transactions extracted based on standards such as those set by TSE by using its transaction trend monitoring system (hereinafter referred to as the "system"). If a transaction is found to have a risk of leading to violation of laws and regulations, etc. as a result of the screening, the Company takes actions, such as conducting an interview or giving a warning (hereinafter referred to as "measures") against the customer, etc. that has conducted the transaction (including proprietary trading), according to the contents of the transaction and the past transaction status of the customer, etc. Under such circumstances, transactions of eight out of the ten issues of shares in the conduct in this case were extracted by the system as those suspected of being unfair transactions. However, as the Company sets a standard to implement the measures when the transactions are conducted over two or more days, transactions like those relating to the conduct in this case, which are conducted only on one market day for each issue, are not made subject to the measures, even if they are extracted by the system.

Moreover, the Company conducts transaction screening for proprietary trading related to specific events, such as block trades, irrespective of whether it is extracted by the system (hereinafter referred to as "event screening"). However, block offers are not made subject to the event screening, even though they involve similar risks as block trades, etc., such as there being an incentive to manipulate the closing price through proprietary trading.

Accordingly, the measures were not implemented for any of the transactions relating to the conduct in this case.

The circumstances above indicate that the Company's control environment for transaction screening is found to be deficient, and they constitute the circumstances provided in Article 123, Paragraph 1, item (xii) of the Cabinet Office Order on Financial Instruments Business (hereinafter referred to as the "FIB Cabinet Office Order") based

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on the provisions of Article 40, item (ii) of the FIEA.

Meanwhile, the circumstances above are found to be attributable to the Company's insufficient recognition of the risks involved in proprietary trading and other matters, as well as to the failure on the part of the Company's management team to respond to the increasing number of transaction screening cases by sophisticating the system and developing the transaction screening framework accordingly.

(3) Deficiency in the control environment for business operations relating to block offers

Upon execution of a block offer, the Company confirms the buying customers' purchase intent in advance. In that process, a considerable number of the Company's sales representatives provide such an explanation which allows buying customers to identify the execution date of the block offer. This situation is found to be giving an opportunity for customers who intend to conduct short selling on the block offer execution date to do so, and is serving as a cause that induces short selling.

Since the time when the introduction of block offers was considered (in 2012), the Company had recognized concerns that buying customers' short selling of the issue subject to the block offer would distort the price formation of the issue. However, the Company had commenced the block offer operations without appropriately discussing a desirable way of providing information to buying customers in relation to the block offer execution date and other matters within the company.

Later, as the Company actually faced falls in share prices of the target issues on block offer execution dates, questions were raised, such as concerns about price formation. Nevertheless, the company has failed to take effective countermeasures against the concerns.

The abovementioned status of the Company's business operations concerning block offers is likely to undermine market fairness, and is found to constitute a situation in which it is "necessary and appropriate in the public interest or for the protection of investors as concerns... business operations" as prescribed in Article 51 of the FIEA.

The situation above is attributable to the fact that the Company lacked awareness as a gatekeeper of the market by prioritizing the promotion of its own business operations and hardly having the awareness to rectify the problems relating to its block offers, and that the company's control environment for appropriately identifying business risks and challenges and taking effective measures, such as reviewing the product features, was

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insufficient. Therefore, the Company's control environment for governance aimed at ensuring appropriate business operations is found to be deficient.

(4) Inappropriate operations of business in cooperation with a bank

Laws provide that a financial instruments business operator engaged in a securities-related business (limited to an operator engaged in a type I financial instruments business) must not receive from, or provide to, its parent corporation, etc. or subsidiary corporation, etc. any undisclosed information on the issuer, etc., unless the issuer, etc. has given prior consent in writing or by means of an electronic or magnetic record on the provision of such undisclosed information by the financial instruments business operator or its parent corporation, etc. or subsidiary corporation, etc. However, from January 2021 through October 2021, the Company received from, or provided to Sumitomo Mitsui Banking Corporation, which is its "parent corporation, etc.," undisclosed information on corporate customers multiple times and shared this information within the Company, while recognizing that suspension of the information sharing was requested by or consent to the information sharing was not obtained from the corporate customers.

The abovementioned conducts of the Company are found to constitute the act prescribed in Article 153, Paragraph 1, item (vii) of the FIB Cabinet Office Order based on the provisions of Article 44-3, Paragraph 1, item (iv) of the FIEA.

Meanwhile, the abovementioned conducts are found whereby officers and employees of the Company prioritized the profit of the Company through obtaining deals, nevertheless recognizing that information cannot be received or provided between the bank and the securities company. Also given that executive managing officers of the Company are found to have been directly involved in receiving undisclosed information and sharing information with the persons concerned within the company, the abovementioned conducts are found to be attributable to the fact that there is a lack of awareness of complying with laws and regulations, etc. in promoting bank-securities business relationships in the Company.

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