

Briefing note
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Market Abuse: European Commission proposes new EU regime

The European Commission has now published its formal legislative proposals for a new Market Abuse Regulation (MAR) and a new Market Abuse Directive (MAD2) to replace the 2003 Market Abuse Directive (MAD). The new Regulation seeks to create a single, directly applicable EU-wide rulebook for market abuse enforced by national administrative sanctions, while the new Directive would require all Member States to introduce criminal sanctions for intentional insider dealing and market manipulation. The new regime would also broaden the coverage of the EU rules in a number of ways, in particular for instruments traded on trading facilities other than regulated markets and for emissions allowances and commodities.

Timing

These proposals are going into the EU legislative process alongside the Commission's other proposals to revise the Markets in Financial Instruments Directive (MiFID2) and for a companion regulation (MiFIR) to which both MAR and MAD2 refer. It is likely that the Council of Ministers and European Parliament will take a year or so to negotiate this package of proposals. On this basis, MAR and MAD2 could be adopted at the end of 2012 but they would only fully take effect two years later, since the proposals give Member States 24 months to address the consequences in their domestic legislation.

In particular, a number of Member States have market abuse regimes which are broader or more stringent than MAD requires (e.g. Ireland, Luxembourg and the UK). It is likely that MAR will signal the end to these national super-equivalent regimes. However, MAD2 envisages that Member States may adopt or maintain more stringent criminal law rules for market abuse and, because of their Treaty rights on criminal law matters, Ireland and the UK can choose whether to opt into MAD2 (which will not apply in Denmark).



Scope

MAD applies to financial instruments admitted to trading on an EU regulated market (as defined in MiFID). MAR extends the scope of the market abuse regime to cover financial instruments admitted to trading on multilateral trading facilities (MTFs) and the new category of organised trading facilities (OTFs), as defined in MiFIR, if they are within the EU. This will significantly extend the scope of insider dealing and market manipulation rules, in particular to cover securities listed on markets outside the EU, many of which are also traded on EU MTFs. In addition,

many OTC derivatives will be traded on OTFs, to meet the platform trading mandate in MiFIR, and so will come within the direct scope of market abuse rules for the first time.

In a similar way to MAD, the insider dealing rules in MAR will apply to trading in financial instruments whose value relates to financial instruments covered by the Regulation (including OTC derivatives on such instruments). MAR specifically indicates that credit derivatives relating to covered securities are also within the scope of the insider dealing rules.

MAR also goes further than MAD by extending the market manipulation rules to cover trading and other behaviour relating to OTC derivatives and other financial instruments which has or is likely or intended to have an effect on financial instruments admitted to trading on EU trading facilities.

The extension of scope will significantly expand the extraterritorial reach of EU market abuse rules, since MAR will apply to insider dealing or market manipulation taking place entirely outside the EU simply because the trading relates to an instrument which happens also to be admitted to trading on a trading facility in the EU - regardless of whether the conduct takes place on an EU trading facility or actually has any effect on EU markets. It will also make it much more difficult for market participants to identify which instruments are covered by EU market abuse rules in the absence of any consolidated list of instruments admitted to trading across all relevant EU trading facilities.

MAR will exempt trading in own shares in buy-back programmes and trading in own shares for stabilisation purposes in accordance with conditions set by implementing measures to be adopted by the Commission, replacing the existing measures under MAD. It is probably an oversight that MAR restricts the safe harbour for stabilisation to trading in own shares, as the MAD exemption applies more broadly.

MAR also contains an extended exemption for behaviour by EU governments, central banks and other institutions (including the European Financial Stability Facility) in pursuit of monetary, exchange rate or public debt management policy (or EU climate policy), but not for non-EU governments or central banks despite the broad extraterritorial reach of the EU rules.

Insider dealing

Like MAD, MAR will prohibit the use of inside information to deal (or attempt to deal) in relevant financial instruments, recommending or inducing another person, on the basis of inside information, to deal in such instruments and the improper disclosure of inside information. However, it would extend the dealing restriction to cover amending or cancelling an order, even if this is done to avoid trading on the basis of inside information.

MAR introduces an explicit defence from the insider dealing prohibition where the information is not used by the individuals concerned in the dealing because it is held on the other side of effective Chinese walls. However, MAR does not otherwise address the uncertainties resulting from the decision of the European Court of Justice in *Spector Photo Group NV v CBFA*. This held that the insider dealing prohibition in MAD applies to anyone who deals in securities while in possession of inside information, even if the information did not influence the trading decision, while acknowledging that the accused may be able to establish unspecified defences (e.g. based on the recitals in MAD which no longer appear in MAR).

MAD defines inside information as non-public information of a precise nature that would be likely to significantly affect the prices of relevant financial instruments. An implementing directive states that this means any information that a reasonable market participant would be likely to use as part of the basis of his investment decision. The debate whether this test supplements or supplants the core definition may continue under MAR as it uses similar words. However, MAR extends the definition of inside information to

include a new category of non-public information that a reasonable investor would regard as relevant when deciding the terms of a transaction. This could extend insider dealing to cover a broad range of information which investors find relevant, even if not precise or price sensitive.

Market manipulation

MAR broadens the existing definition of market manipulation. It extends the definition to cover all behaviour, not just transactions and orders to trade, that may give false or misleading signals or secure prices at artificial levels or that employ fictitious devices, deceptions or contrivances. It removes the possibility of establishing a defence based on accepted market practices (subject to a one year transitional period for previously notified practices). It also prohibits attempts to engage in market manipulation.

In addition, MAR extends the list of examples of presumed market manipulation to include the case where orders are sent to a trading venue, by means of algorithmic or high frequency trading, without an intention to trade but for the purpose of disrupting or delaying the trading system, making it more difficult for others to identify genuine orders or creating a false or misleading impression of supply or demand.

Disclosure

MAR will continue to require issuers of securities to inform the public as soon as possible of inside information which directly concerns them, but this duty will not extend to the new category of non-price sensitive relevant information.

An issuer will still be able to delay publication to protect its legitimate interests, if the omission would not be

likely to mislead the public and the issuer can keep the information confidential. However, MAR will require the issuer to inform the competent authority of the delay immediately after the information is published. In addition, the competent authority will be able to authorise the delayed disclosure of systemically important information in the public interest.

The disclosure obligation does not apply to issuers who have not approved trading of their financial instruments on an EU regulated market, MTF or OTF.

Emissions allowances and commodities

MAR extends the market abuse rules to cover EU emissions allowances (and related products). It also requires all participants in the allowances market to disclose publicly any inside information about allowances they hold relating to their group's business or facilities.

MAR extends the scope of the market manipulation (but not insider dealing) rules to cover behaviour relating to underlying spot commodity contracts (but not wholesale energy products) affecting financial instruments admitted to trading on EU facilities. It also states that it covers behaviour in financial instruments (whether or not traded on EU facilities) that affect any spot commodity contract.

MAR extends the definition of inside information relating to commodity derivatives by applying broadly the same definitions as apply to other financial instruments, so that all price sensitive or relevant information is inside information even if not disclosable to the market. However, there is no statement that information as to a market participant's own plans and strategies for trading should not be considered as inside information (unlike the new EU Regulation on Wholesale Energy Market Integrity and Transparency).



Other issues

MAR largely reproduces the existing framework in MAD regulating insider lists, manager reporting, suspicious transaction reports and investment research. However:

- **Insider lists:** These obligations will not apply to issuers whose financial instruments are admitted to trading on the new SME growth market category under MiFID2.
- **Manager reporting:** MAR states that reporting of managers' transactions should cover the pledging or lending of shares, trading by portfolio managers on behalf of the manager and trading in emissions allowances by a manager of an emissions allowance market participant. MAR also sets a harmonised threshold for reporting at €20,000 per year.
- **Suspicious transactions:** MAR extends the duty to report to cover suspicious orders as well as transactions.
- **Implementing measures:** There will be new implementing or delegated acts to define the scope of these requirements. This will mean, for

example, directly applicable harmonised EU rules on the content of insider lists and research disclosures.

Enforcement

MAR requires Member States to implement effective, proportionate and dissuasive rules on administrative measures and sanctions for breach of MAR, including fines of up to at least €5m for individuals or 10% of turnover for undertakings. Fining policy must take account of a range of specified factors, including the profit or loss made or avoided and the level of cooperation with the authorities.

There are extensive provisions aimed at achieving greater co-ordination between Member States on investigations and enforcement. Member States must put in place provisions to protect whistleblowers and are permitted to grant money rewards.

Under MAD2, insider dealing and market manipulation would constitute a criminal offence when committed intentionally, as would inciting, aiding and abetting, and attempts to commit these offences. A legal person may also be held liable where the offence was committed for their benefit by a person who has a leading position within the legal person.

Contacts

If you would like to know more about the subjects covered in this publication or our services, please contact:



Chris Bates

Partner

T: +44 20 7006 1041

E: chris.bates@cliffordchance.com



Marc Benzler

Partner

T: +49 697199 3304

E: marc.benzler@cliffordchance.com



Carlos Conceicao

Partner

T: +44 20 7006 8281

E: carlos.conceicao@cliffordchance.com



Caroline Dawson

Lawyer

T: +44 20 7006 4355

E: caroline.dawson@cliffordchance.com



Hannah Ellwood

Senior Associate

T: +44 20 7006 8844

E: hannah.ellwood@cliffordchance.com



Frédéric Lacroix

Partner

T: +33 14405 5241

E: frederick.lacroix@cliffordchance.com



Charles Morris

Senior Associate

T: +44 20 7006 8288

E: charles.morris@cliffordchance.com



Patrick Sarch

Partner

T: +44 20 7006 1322

E: patrick.sarch@cliffordchance.com

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