

CMS Banking and Finance webinars

Market Abuse Directive II

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Your hosts for today's webinar



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CMS webinar: MAD II

The changes

Looking at...

1. The current basics – a quick look at the key uncertainties
2. The case for change
3. The new structure
4. Criminalisation – the policy and the proposals
5. Are we heading towards convergence or divergence?
6. The possible impact of the changes

Market abuse is...

1. **Behaviour** by one or more **persons**, with no intent needed
2. Relating to **qualifying investments** on a **prescribed market**



Shares, bonds, CIS units, related instruments



EU

3. Occurring **in the member state**, or **listed there**

Market abuse – key behaviours & uncertainties

Insider dealing

1. Did you act – deal/require/tip off?
2. Did you have inside information?
 - a) Precise = probability + price
 - i. Exists or reasonably expected
 - ii. Can conclude price effect
 - b) Not generally available
 - c) Reasonable investor likely to use
3. Did you deal on the basis of it?

Other market abuse conduct

1. Tipping off
 2. Market Manipulation
 3. Dissemination of information
- And additional member-state specific offences

Is the regime working (at least in the UK)?

FCA: Occasional Paper No. 4: Why has the FCA's market cleanliness statistic for takeover announcements decreased since 2009? (July 2014)



So what's the case for change?

Criminalisation

1. Integrated & efficient market requires integrity
2. NCAs do not possess full or consistent fining powers
3. Not successful to date
4. Financial crisis showed widespread abuse
5. Criminal sanctions will send appropriate message for serious cases

So what's the case for change?

The Regulation

1. Problems which have **negative impacts** in terms of market integrity and investor protection, lead to an unlevel playing field and result in compliance costs and disincentives for issuers.
2. Regulatory, market and technological **developments cause gaps** in the regulation of new markets, platforms and OTC instruments.
3. Numerous **options and discretions** in MAD, as well as a lack of clarity on certain key concepts, undermines the effectiveness of the Directive.
4. Divergence of **national laws** creates obstacles to trade and significant distortions of competition. A uniform framework is needed to preserve market integrity, avoid regulatory arbitrage and provide more legal certainty and less legal complexity.

The new structure will apply from July 2016

The Directive

- Criminal sanctions
 - Insider dealing
 - Market manipulation

The Regulations

- Directly applicable
- All the current provisions
- Plus some key additions

The main key changes

- The Regulations extend to financial instruments
 - traded on MTFs and on OTF or
 - which depend on OTC traded instruments
- Tighter definition of precise & price effect
- Disclosure requirements and insider list management

Criminal Sanctioning of Market Abuse: Status Quo

- Some forms of serious breaches of national laws implementing MAD not subject to criminal sanctions in all Member States
- No union-wide understanding of what constitutes a "serious breach"
- Example Germany:
 - Completed cases of intentional market manipulation, insider trading and the making available of inside information or inducing or recommending transactions on the basis of inside information by certain qualified individuals are subject to imprisonment of up to five years or a criminal fine.
 - German criminal law does not provide for the punishment of legal persons.

CRIM-MAD

- Bases on Article 83 (2) of the Treaty on the Functioning of the European Union: "*If the approximation of criminal laws and regulations of the Member States proves essential to ensure the effective implementation of a Union policy in an area which has been subject to harmonisation measures, directives may establish minimum rules with regard to the definition of criminal offences and sanctions in the area concerned.*"
- Launched complaints (e.g. by the German *Bundesrat*) claiming a lack of competence of the EU were not successful

CRIM-MAD - Criminalisation

- Requires Member States to ensure that insider dealing, recommending or inducing another person to engage in insider dealing and market manipulation (as defined in the CRIM-MAD) constitutes a criminal offence in serious cases and when committed intentionally.
- Market Manipulation: Intentionally (a) giving false/misleading signals of supply/demand/price; (b) securing price of financial instrument at abnormal/artificial level; (c) trading using a fictitious device/deception/contrivance; (d) disseminating information giving false/misleading signal in serious cases – similar tests; (e) giving false/misleading information or providing false or misleading input manipulating the calculation of a benchmark.

CRIM-MAD - Criminalisation

- Insider dealing: Intentionally (i) using inside information to deal or cancel or amend an existing order or (ii) intentionally recommending or inducing another person, at least in serious cases
- Inciting, aiding and abetting and attempt shall also be punishable as criminal offence.
- Above Offences are to be punished with a maximum term of imprisonment of four years for natural persons.
- Member States need to assure that legal persons can be held liable for market manipulation committed by certain of "leading persons".
- Member States are free to implement a stricter regime.

CRIM-MAD – Impact of Implementation

- Significant change expected for Member States in which market manipulation is not subject to criminal sanctions, as new players will be applying new rules
- Example Germany:
 - Criminalisation is extended to cases of attempted insider offences and market manipulation
 - The requirement to hold legal persons liable for serious cases of market manipulation or insider offences by representatives is not expected to require the introduction of a novel corporate criminal law regime.
 - Current maximum term of imprisonment of up to five years already in line CRIM-MAD requirements

CRIM-MAD – Impact of Implementation

- Most significant impact in Germany expected from administrative pecuniary sanctions of market manipulation under MAR:
 - Natural persons: Up to EUR 5 million
 - Legal persons: Up to EUR 15 million or three times annual turnover
 - 15% of the profits gained because of the infringement
- Current situation in Germany:
 - Criminal pecuniary sanctions of up to EUR 1 million
 - Sanctions administered are in most cases significantly below EUR 1 million.

MAR, CRIM-MAD – Steps towards Harmonisation

- With the MAR, the rules on
 - market manipulation, insider dealings, fast disclosure and directors' dealings,
 - competencies of national regulators and ESMA , and
 - administrative measures and sanctionsbecome European law which is directly applicable in the Member States.
- MAR has a significantly higher level of detail than the 2003 MAD
- CRIM-MAD provides for European law on the criminal sanctioning of market abuse for the first time

MAR, CRIM-MAD – Sources of Divergence

- Enforcement not in the hands of an European authority, but still with national regulators that may interpret MAR differently
- Various different language versions may give rise to differing interpretation
- It seems difficult to establish the legislators' intent for purposes of interpreting MAR due to a mass of documents from Commission, Council and Parliament

MAR, CRIM-MAD – Sources of Divergence

- Administrative sanctioning and measures only provide for minimum requirements
- CRIM-MAD requires implementation into national law in a field (criminal law) which is not harmonised
- National rules on criminal procedures vary greatly
- Denmark and UK do not apply CRIM-MAD

MAR, CRIM-MAD – Tools for Harmonisation/Homogenisation

- Level 2: MAR empowers the Commission to adopt seven delegated acts and requires ESMA to issue six regulatory technical standards and seven implementing technical standards to be adopted by the Commission.
- Level 3: MAR requires ESMA to issue guidelines and recommendations in three cases.

How different will daily life actually be?

Criminalisation – the impact

- Requires criminal trial
 - Criminal process & protections
 - Criminal standard of proof
- Wide scope
 - In the UK nearly all market abuse cases are for intentional market abuse and are serious
 - Inclusion of ancillary offences extends to administrative processes
 - Significant potential impact on firms
- Will be considerable divergence
 - Different processes & penalty policies
 - Not UK or Denmark
 - Member states may add recklessness and negligence

The difference in the civil arena

OLD WORLD

Market abuse

- **Behaviour** by one or more **persons**
- No intent needed
- Relating to **qualifying investments** on a **prescribed market**
- Occurring **in the MS** or **MS listed**

NEW WORLD

Insider dealing & market manipulation

- Any **behaviour or transaction**
- No intent needed
- Relating to **financial instrument** on a **regulated market** or **MTF** or **OTF**
- Occurring **anywhere**

Market abuse – insider dealing

OLD WORLD

1. Did you act – deal/require/tip off?
2. Did you have inside information?
 - a) Precise =
 - i. Exists or reasonably expected +
 - ii. Can conclude price effect
 - b) Not generally available
 - c) Reasonable investor likely to use
3. Did you deal on the basis of it?
 - a) Or it was a contributory element

NEW WORLD

1. Did you possess it?
2. Did you use? – same + cancel, amend
3. Was it inside information re issuer?
 - a) Precise = unchanged;
 - b) Not made public & if made public likely significant price effect;

Market manipulation

OLD WORLD

- a) Trade for illegitimate reason
- b) Giving false or misleading impression or
- c) Secures prices at abnormal level

NEW WORLD

- a) Deal, trade or behaviour (or attempt)
 - i. Gives false or misleading signals supply/demand/price or
 - ii. Secures prices at abnormal level
 - iii. Unless accepted market practice
- b) Deal, trade or behaviour using fiction, deception or contrivance
- c) Disseminating false/misleading information => (a)

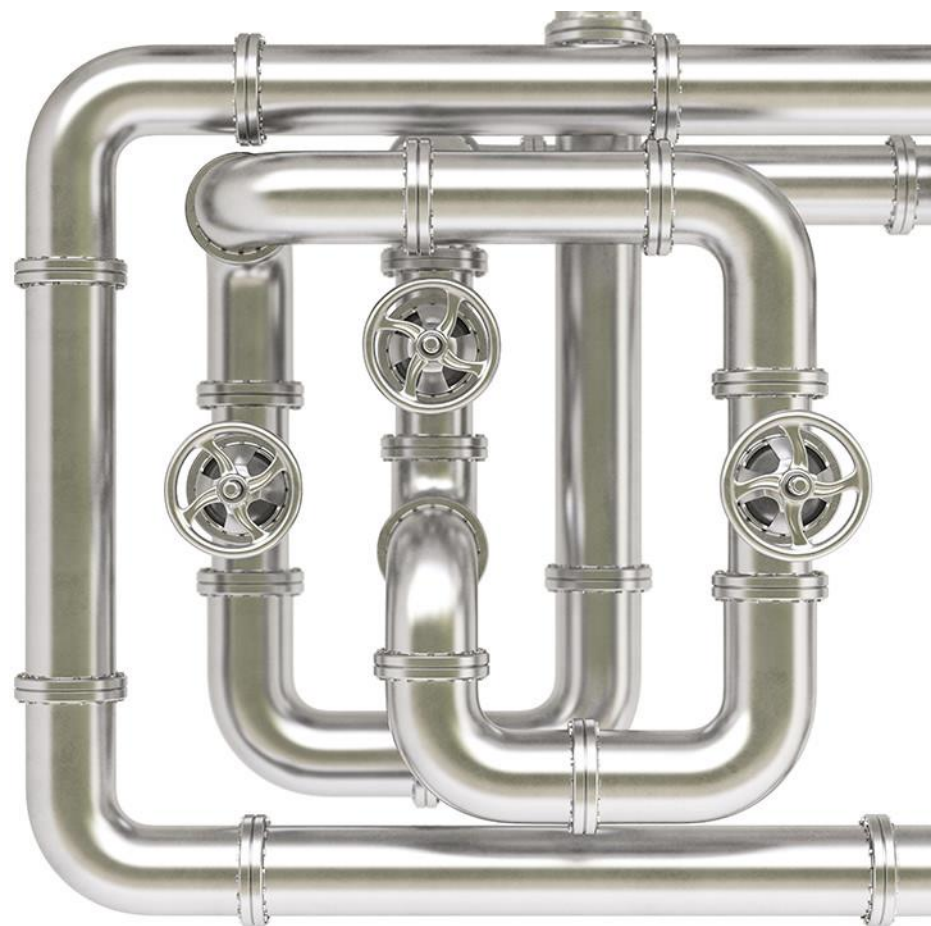
Examples given in Annex

So what?

- Criminalisation
 - Impact on a firm
 - Integrity of traders
 - Oversight of managers
- Extension of civil regime
- Greatest effect in non-core jurisdictions?
- Refresh procedures & training

Q&A

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YOUR
QUESTIONS



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