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Briefing Note

Market Abuse Regulation

The new Market Abuse Regulation (MAR)[1] takes effect on 3 July 2016. While many aspects of the new market abuse regime are similar to the existing UK regime, there are some important and substantive changes. Issuers who have not already done so will need to review their existing policies and procedures as soon as possible.

This note is intended to give a brief overview of some of the key changes under the new market abuse regime as it applies to issuers.

BACKGROUND

The current market abuse regime in the UK implements the Market Abuse Directive (MAD) and came into force on 1 July 2005. Following a review of the market abuse regime across Europe, MAD is being replaced and repealed by the Market Abuse Regulation (MAR) and takes effect on 3 July 2016.[2]

MAR is intended to enhance market integrity and investor protection by harmonising the rules on market abuse across the EU. MAR targets unlawful behaviour in the financial markets including insider dealing, unlawful disclosure of inside information and market manipulation.

MAR is directly effective in the UK and other EU member states. At the EU level, various delegated acts, technical standards and guidance will sit alongside MAR itself. While most of the delegated acts and technical standards have now either been finalised or are near-final form, it is not clear whether all of the relevant items will be in absolute final form by 3 July 2016.

At the UK level, relevant changes to primary and secondary legislation are being made, the Financial Conduct Authority (FCA) has published Policy Statement PS16/13 (April 2016) setting out changes that will be made to the FCA Handbook, and the London Stock Exchange has published AIM Notice 44 (April 2016) setting out proposed changes to the AIM Rules as well as an edition of its Inside AIM newsletter focussing on MAR.

In light of requests for further guidance in responses to its earlier consultation papers, the FCA has highlighted a number of areas it is considering further. Issuers will need to continue to monitor developments.

SCOPE OF THE NEW MARKET ABUSE REGIME

The scope of the market abuse regime is being extended to cover new markets and new financial instruments. As well as financial instruments admitted to trading, or in respect of which an application for admission to trading has been made, on regulated markets (such as the main market of the London Stock Exchange), MAR extends to financial instruments admitted to trading, or in respect of which an application for admission to trading has been made, on multi-lateral trading facilities (MTFs), as well as instruments traded on organised trading facilities (OTFs). The extension of the new regime to issuers with securities admitted to trading on MTFs means that the new regime will apply to AIM companies.

1 596/2014/EU

2 The provisions of MAR relating to organised trading facilities (OTFs), emission allowances and auctioned products based on emission allowances will not take effect on 3 July 2016 and will come into force at a later date. These areas are outside the scope of this note.

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INSIDE INFORMATION

The new regime governing inside information under MAR is broadly similar to the existing UK regime.

Inside information

MAR defines "inside information" as information of a precise nature which has not been made public relating directly or indirectly to one or more financial instruments, and which, if it were made public, would be likely to have a significant effect on the prices of these financial instruments or on the price of related derivative financial instruments.

Information is deemed to be of a precise nature if it indicates a set of circumstances which exists or which may reasonably be expected to come into existence, or an event which has occurred or which may reasonably be expected to occur, where it is specific enough to enable a conclusion to be drawn as to the possible effect of that set of circumstances or event on the prices of the financial instruments or related derivatives financial instrument.

Information would be likely to have a significant effect on price if it is information a reasonable investor would be likely to use as part of the basis of his or her investment decisions.

Disclosure of inside information

Under MAR, issuers are required to publish inside information as soon as possible. Inside information must be made available on the issuer's website for at least five years (the date and time of disclosure should be clearly indicated and disclosures should be organised in chronological order). The disclosure of inside information should not be combined with the marketing by the issuer of its activities.

Delaying disclosure of inside information

An issuer can delay disclosure of inside information if the following conditions are satisfied, namely, (i) immediate disclosure is likely to prejudice the legitimate interests of the issuer, (ii) delayed disclosure is not likely to mislead the public, and (iii) the issuer is able to ensure the confidentiality of the information.

Where the confidentiality of inside information is no longer ensured (including situations where a rumour is sufficiently accurate to indicate that confidentiality is no longer ensured), the issuer must make an announcement as soon as possible.

Where inside information is disclosed to a third party in the normal course of exercise of employment, profession or duties, the person receiving the information must owe a duty of confidentiality (whether based on law, contract or articles of association). Otherwise, such information must be announced simultaneously in the case of intentional disclosure and promptly in the case of non-intentional disclosure.

Where an issuer has delayed the disclosure of inside information, it is required to inform the FCA about the delay immediately after the information is disclosed to the public.[3] In addition, at the request of the FCA, an issuer must provide the FCA with a written explanation of how the conditions referred to above were met. Issuers are also required to comply with detailed record-keeping requirements where the disclosure of inside information has been delayed – the precise requirements are quite burdensome and compliance with them may prove challenging for issuers.

The European Securities and Markets Authority (ESMA) published a consultation paper (ESMA 2016/162) in January 2016 setting out draft guidelines on the legitimate interests of the issuer for delaying disclosure of inside information (such as when the issuer is conducting negotiations, where the outcome of such negotiations would be jeopardised by immediate public disclosure of the information) and when delaying disclosure is likely to mislead the public. The ESMA guidelines have not yet been finalised, and the FCA has indicated that it will consider the status and continuance of the amended DTR 2.5 (*Delaying disclosure of inside information*) in due course once there is more certainty on the content of the guidelines.

AIM

AIM companies will fall within the ambit of the MAR inside information regime from 3 July 2016. As a result, AIM companies will be subject to two disclosure regimes - the provisions on inside information under MAR and the provisions on price sensitive information under AIM Rule 11. They will also have two regulators - the FCA as competent authority under MAR and AIM Regulation for AIM.

In its April 2016 Inside AIM newsletter, AIM indicated that AIM companies must consider the two sets of obligations separately and that compliance with MAR does not mean that an AIM company will have satisfied its obligations under the AIM Rules. Specifically, in considering whether they are able to delay the disclosure of inside information, AIM companies need to consider the position under both the MAR regime and the AIM Rules.

3 The form to be used was published by the FCA in its Primary Markets Bulletin 15 on 25 May 2016 and is available here http://www.fca.org.uk/static/documents/forms/delayed-disclosure-inside-information-form.pdf

Action to be taken
Issuers should review their processes and procedures for handling and disclosing inside information in light of the new MAR regime. AIM companies will need to consider their MAR obligations alongside their disclosure obligations under the AIM Rules.

INSIDER LISTS

The position in relation to insider lists under MAR is similar to the current position set out in DTR 2.8 (*Insider lists*), though the prescribed information to be included in insider lists has become more onerous.

Issuers must draw up a list of persons who have access to inside information, keep the list up-to-date, and provide a copy to the FCA as soon as possible on request.

Issuers (and persons acting on their behalf) must take all reasonable steps to ensure that each person on the insider list acknowledges in writing the legal and regulatory duties entailed and is aware of the sanctions applicable to insider dealing and unlawful disclosure of inside information.

Where a person other than the issuer maintains the insider list, the issuer remains fully responsible for it and must always have the right to access the list. The FCA is considering whether an adviser's adviser can keep its own list or whether an issuer's adviser has to maintain the list for its advisers.

Insider lists should be divided into sections for each piece of deal-specific or event-based inside information. There can also be a separate section for permanent insiders (persons who, due to the nature of their function or position, have access to all inside information within the issuer).

Insider lists should be kept in electronic format and ensure that confidentiality is maintained by restricting access to a limited number of identified persons. Insider lists should be promptly updated where there is a change in the reason for including someone on the list, or where a new person is added to the list, or where someone ceases to have access to the information. Each update should specify the date and time when the change triggering the update occurred.

Insider lists should be kept by issuers (or persons acting on their behalf) for at least five years.

AIM

AIM companies will be brought within the ambit of the insider list regime from 3 July 2016. There are more relaxed rules on insider lists for issuers whose financial instruments are admitted to trading on an SME growth market. While AIM may become an SME growth market down the line, the SME growth market regime will not come into force until MiFID II is implemented (expected January 2018). AIM companies will need to comply with the MAR insider list regime in the meantime.

Action to be taken
Main market companies will need to review and update their procedures for maintaining insider lists and the related templates. AIM companies will need to put in place procedures for maintaining insider lists and adopt the related templates.

MARKET ABUSE OFFENCE

The market abuse offence under MAR is similar to the existing UK civil offence of market abuse.

Existing UK regime

The existing UK regime is set out in Part VIII of the Financial Services and Markets Act 2000 (FSMA). Section 118 identifies six behaviours which constitute market abuse: (i) insider dealing, (ii) unlawful disclosure of inside information, (iii) market manipulation, (iv) market deception, (v) dissemination of false or misleading information and (vi) misleading behaviour / market distortion. Currently, the Code of Market Conduct set out in the FCA Handbook gives guidance on whether or not specific types of behaviour amount to market abuse. The existing market abuse offices in FSMA are being repealed and replaced by the MAR market abuse offences referred to below.

By way of reminder, the UK civil market abuse regime sits alongside the UK criminal regime, that is, the provisions on insider dealing set out in Part V of the Criminal Justice Act 1993 and the provisions on misleading statements and misleading impressions set out in sections 89 and 90 of the Financial Services Act 2012.

Market abuse under MAR

Under MAR, it is an offence to (i) engage or attempt to engage in insider dealing, (ii) recommend that another person engages in insider dealing or induce another person to engage in insider dealing, (iii) unlawfully disclose inside information or (iv) engage or attempt to engage in market manipulation. There are safe harbours for buyback programmes and stabilisation measures conducted in accordance with the relevant rules. Where the insider dealing and market manipulation offences are committed by a legal person, they are also committed by any natural person who participated in the decision to carry out the activities.

Insider dealing
Insider dealing arises where a person possesses inside information and uses that information by acquiring or disposing of, for its own account or for the account of a third party, directly or indirectly, financial instruments to which that information relates. It is also insider dealing to cancel or amend an order to which inside information relates where the order was placed before the person possessed the information.

Legitimate behaviours
In relation to insider dealing and unlawful disclosure of inside information, MAR sets out certain "legitimate behaviours" although the rules can still be infringed if it is established that there was an illegitimate reason for the trade or behaviours concerned.

Market manipulation
Market manipulation comprises: (i) false or misleading behaviour, (ii) behaviour which secures, or is likely to secure, the price of financial instruments at an abnormal or artificial level, (iii) deceptive behaviour, (iv) dissemination through the media, including the internet, of false or misleading information which the person knew or ought to have known was false or misleading and (v) manipulation of benchmarks. MAR Annex I gives non-exhaustive indicators of items (i), (ii) and (iii). MAR also sets out certain behaviours which are considered to be market manipulation.

NEW MARKET SOUNDINGS SAFE HARBOUR

As noted above, it is an offence to unlawfully disclose inside information. Unlawful disclosure of inside information occurs where a person discloses inside information other than in the normal exercise of an employment, profession or duties.

MAR creates a new safe harbour for the disclosure of inside information in the course of market soundings.

Market soundings comprise the communication of information, prior to the announcement of a transaction, in order to gauge the interest of potential investors in a possible transaction and the conditions relating to it such as its potential size or pricing. There are separate provisions in MAR dealing with market soundings in the context of takeovers.

When conducting market soundings, the disclosing market participant (DMP) must consider whether the market sounding will entail the disclosure of inside information, make a written record of its conclusion and the reasons for it, and provide the written records to the FCA on request. This applies to each disclosure of information in the course of the market sounding and the records should be updated accordingly.

Detailed procedural and record-keeping requirements

Before making the disclosure, the DMP should: (i) obtain the consent of the recipient, (ii) inform the recipient that he is prohibited from using, or attempting to use, that information, by acquiring or disposing of for his own account or for the account of a third party, directly or indirectly, financial instruments relating to that information, (iii) inform the recipient that he is prohibited from using that information, or attempting to use that information, by cancelling or amending an order which has already been placed concerning financial instruments to which the information relates, (iv) inform the recipient that he is obliged to keep the information confidential and (v) keep a record of all information given to the recipient and the identity of the potential investors (including legal and natural persons acting on behalf of potential investors) and the date and time of each disclosure (and provide that record to the FCA on request).

When inside information disclosed in the course of a market sounding ceases to be inside information, the DMP must inform the recipient as soon as possible (and keep a record).

Records kept in accordance with the provisions on market soundings must be kept for five years and disclosed to the FCA on request.

The proposed EU Commission Delegated Regulation and Implementing Regulation relating to market soundings set out in greater (and considerable) detail the procedures to be followed, and records to be kept, in connection with the conduct of market soundings.

The person receiving the market sounding must assess for itself whether it is in possession of inside information or when it ceases to be in possession of inside information. ESMA consultation paper ESMA 2016/162 (January 2016) sets out draft guidelines for persons receiving market soundings.

Action to be taken
Issuers should consider whether they need to put in place processes and procedures in relation to market soundings.

TRANSACTIONS BY PDMRS AND CLOSELY ASSOCIATED PERSONS

Persons discharging managerial responsibilities (PDMRs), and persons closely associated with them, are required to notify the issuer and the FCA of all transactions conducted on their own account in shares or debt instruments of the issuer or related derivatives or financial instruments.

The notification should be made promptly and within three business days (not the current four business days) after the date of the transaction. The obligation to notify kicks in once the total amount of transactions exceeds a new *de minimis* threshold of €5,000 within a calendar year. The FCA has indicated that it is considering how the aggregation of transactions is calculated to determine if the €5,000 threshold has been reached and also the exchange rate to be used for the calculation. The FCA has indicated that issuers, PDMRs and their closely associated persons may continue to disclose, on a voluntary basis, all transactions, regardless of threshold, if they wish to do so.

The issuer is required to announce the information contained in the above notification promptly and within three business days of the transaction date. The FCA is considering these reporting requirements given that the PDMR and the issuer are both subject to the same three day notification period from the transaction date.

Issuers are required to notify PDMRs of their obligations under Article 19 (*Managers' transactions*) of MAR in writing. PDMRs are, in turn, required to notify persons closely associated with them of their obligations under Article 19 in writing and to keep a copy of the notification. Issuers are also required to draw up a list of all PDMRs and persons closely associated with them.

Closed periods

There is a new MAR closed period of 30 days before the announcement of an interim financial report or year-end report. PDMRs are prohibited from conducting transactions during a closed period of 30 days before the announcement of an interim financial report or year-end report, except in certain limited circumstances.[4]

An issuer may allow a PDMR to trade during a closed period (i) in exceptional circumstances, such as severe financial difficulty, or (ii) due to the characteristics of the trading involved for transactions made under or related to an employee share or saving scheme, qualification, or entitlement of shares, or transactions where the beneficial interest in the relevant security does not change.

Closed periods and preliminary announcement of annual results

Under the current UK regime, an issuer's close period is ended by the publication of its preliminary results[5] ahead of its final year-end results. As the MAR provisions on closed periods do not expressly refer to preliminary results announcements, there has been some uncertainty around whether issuers will continue to come out of closed periods on the publication of their preliminary results.

On 26 May 2016, the FCA indicated that the relationship between MAR closed periods and preliminary results was still being discussed at a European level. Pending clarification from the European Commission and ESMA, the FCA will continue to take the view that where an issuer announces preliminary results the closed period, where dealing is prohibited, is immediately before the preliminary results are announced (assuming the preliminary results announcement contains all inside information expected to be included in the year-end report).

Deletion of Model Code

The Model Code set out in Annex 1 to Listing Rule 9 is being deleted as incompatible with MAR. Recognising the role of the Model Code in setting a benchmark and a consistent approach for PDMR trading, in its November 2015 consultation paper the FCA indicated that it would replace the Model Code with rules and guidance on systems and internal procedures for companies and PDMRs applying for clearance to deal. This led to concerns that issuers would end up with a two tier approach to PDMR dealings and closed periods – a MAR closed period regime and a "super-equivalent" FCA regime for dealings outside MAR closed periods. As a result, the FCA dropped the proposal to replace the Model Code in Policy Statement PS16/13 (April 2016).

It has, nonetheless, been suggested that a standard dealing code applying to PDMR dealing outside the MAR closed periods should follow the Model Code as far as possible and could be produced by an industry body. The FCA has indicated that it would support the development of industry-led codes or best practice.

4 MAR uses the term "closed period"; the existing UK regime uses "close period". Under the Model Code, a main market company is currently in a close period for the period of 60 days prior to the publication of a preliminary announcement of its annual results, annual report, half-yearly report and, if relevant, the 30 day period prior to the publication of quarterly results. Under the AIM Rules, an AIM company is currently in a close period for the two months preceding the publication of its annual accounts and half-yearly report and, if relevant, the one month period preceding the publication of quarterly results.

5 For AIM companies this requires the prior approval of AIM Regulation.

AIM

In view of the overlap between AIM Rule 21 (*Restriction on deals*) and the MAR provisions on transactions by PDMRs and closely associated persons, the existing provisions of AIM Rule 21 and the associated guidance are being replaced.

There will be a new requirement for AIM companies to have a share dealing policy for directors and applicable employees. There will be prescribed minimum content requirements for the share dealing policy and AIM companies are expected to update their existing policies by 3 July 2016.

AIM has emphasised that the requirements of the new AIM Rule 21 are separate from the MAR requirements and, accordingly, compliance with MAR will not automatically mean compliance with the AIM Rules.

The requirement under AIM Rule 17 (*Disclosure of miscellaneous information*) to announce directors' dealings without delay is being removed and the notification obligations under MAR will apply to AIM companies from 3 July 2016.

Action to be taken
Main market companies should update their processes and procedures for transactions by PDMRs and their closely associated persons, including their procedures for transactions outside a MAR close period (pending the production of industry-led guidance). AIM companies should likewise update existing (or adopt new) share dealing codes that comply with MAR and the AIM Rules (as amended). Issuers will need to identify their PDMRs and closely associated persons and inform PDMRs of their obligations in writing (PDMRs will, in turn, need to inform their closely associated persons of their obligations in writing).

CHANGES TO FSMA AND PENALTIES

The existing sections 118 to 122 (*market abuse*) of FSMA are to be repealed. The penalties for breach of the market abuse offences under the new MAR regime are to be set out in an amended section 123 and will remain largely unchanged (unlimited fine and/ or public censure). The FCA will also be able to impose penalties for breach of certain new information-gathering powers to be given to it under sections 122A to 122H of FSMA. The FCA's power to suspend trading will be set out in section 122I.

This note is intended to reflect the position as at May 2016. It is intended to give a brief overview of some of the key changes to the market abuse regime. It is not exhaustive and does not constitute legal advice. For further information or specific advice please get in touch with your usual contact at Shepherd and Wedderburn or any of the contacts overleaf.

Summary of headline items

- **Scope of the market abuse regime** – Regime is being widened to include new markets (including AIM) and new financial instruments.
- **Inside information** – New regime for inside information is broadly similar to the existing regime.
- **Delaying disclosure of inside information** – There are new procedures and record-keeping requirements for issuers. Where disclosure of inside information has been delayed, the FCA must be informed about the delay when the information is disclosed to the public and, if requested, the issuer must provide the FCA with a written explanation of how the conditions required to be satisfied to justify the delay were met.
- **Insider lists** – New regime for insider lists is broadly similar to the existing UK regime. There are, however, new (somewhat onerous) prescribed contents for insider lists.
- **Market abuse offence** – Existing civil offence of market abuse in the FSMA is being repealed and replaced with new (albeit similar) market abuse offences under MAR.
- **Market soundings** – New safe harbour to the market abuse offence of unlawfully disclosing inside information where the disclosure is made in the course of market soundings (where information is communicated to potential investors prior to the announcement of a transaction).
- **Transactions by PDMRs and closely associated persons** – New MAR regime for transactions by PDMRs and closely associated persons requires transactions to be notified to the issuer and the FCA within three business days. New *de minimis* threshold of €5,000 within a calendar year, though issuers may continue to require the notification of all transactions. New requirements to identify PDMRs and their closely associated persons and to inform them of their obligations. Model Code being deleted from the Listing Rules. Issuers will need to consider their policy and procedures for dealings clearances.
- **Closed period** – New MAR closed period of 30 days before the announcement of an interim financial report or year-end report.
- **FCA Handbook** – Significant changes being made to relevant parts of the FCA Handbook, with many provisions being replaced by sign-posts to provisions of the relevant EU legislation.
- **AIM** – AIM companies being brought within the MAR regime. Consequential changes being made to AIM Rules, including replacing the existing provisions of AIM Rule 21 (*Restriction on deals*). AIM companies will need to comply with both the AIM Rules and the MAR regime where relevant.
- **Policies and procedures** – Issuers should review their current policies and procedures and ensure that they have appropriate arrangements and document templates in place from 3 July 2016.

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