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June 2003

Dear Mr Demarigny

CESR Consultation Paper on Additional Level 2 Implementing Measures for the Insider Dealing and Market Manipulation Directive

The CBI is a membership organisation, which represents UK companies and others (including both EU and non-EU companies) based in the UK. With direct corporate membership employing over four million and trade association membership representing over six million of the UK workforce, the CBI is the premier organisation speaking for companies in the UK and is also the UK member of UNICE, the European employers' federation. We have responded to a previous CESR consultation on this directive and a copy of our response is attached for ease of reference.

On the current consultation, we believe that market practices should be assumed to be acceptable unless there are grounds for thinking that they are abusive. Otherwise it would be impossible to innovate, which would harm Europe's competitiveness. We are concerned that what is acceptable in one EU country may not be so in all others; as long as companies are complying with the practices of their home jurisdiction then they should not be subject to the assumption that these are not acceptable elsewhere.

Our main concern, however, with the current consultation is the approach to insider lists, which seems overly bureaucratic and not commercially practical. We agree with the approach and wording proposed by the response by the British Bankers' Association, that the focus should be not only on the legal requirements and policy objectives of the directive, but also on the most practical way of achieving these objectives with minimum disruption to companies and their advisers.

Suggesting that companies employ a dedicated resource such as a compliance officer in order to comply with these proposals shows a lack of cost / benefit awareness in accordance with European principles on governance, which is overly focussed on companies employing large



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numbers of people, rather than taking into account the needs of all companies. CESR's advice should be relevant to companies of all sizes.

Companies do not currently produce insider lists in the way suggested by CESR and to do so would create much additional work without equivalent benefits. The focus should be on creating permanent lists or lists for specific transactions, not for a specific piece of inside information. Otherwise any lists produced will be confusing and then may not be correctly produced at all. The content of the lists should be kept as simple as possible which will be more likely to ensure compliance, limited to the name and date of the person in possession of the inside information.

When dealing with advisers outside the company such as lawyers, accountants, etc., issuers would expect them to be bound by professional rules of conduct to manage the handling of inside information among their own people and to manage their own lists. We do not think that issuers should have to keep lists of those outside the company with the possible exception of those with regular access such as audit or law firm partners. The list should only have to be provided to the competent authority on request.

We hope that these proposals will be revised and we remain at your disposal for any questions.

Yours etc.

Susannah Haan

cc. Nigel Phipps, FSA

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14 October 2002

Dear Mr Demarigny

CBI response to CESR consultation on insider dealing & market manipulation

We are grateful for the opportunity to respond to CESR's consultation on possible Level 2 measures for the draft directive on insider dealing and market manipulation (the "Directive"). We support the aims of the Financial Services Action Plan, although we have had concerns about the original lack of consultation on this directive. This makes the current consultation all the more important.

The CBI is a membership organisation, which represents UK companies and others (including both EU and non-EU companies) based in the UK. With direct corporate membership employing over four million and trade association membership representing over six million of the UK workforce, the CBI is the premier organisation speaking for companies in the UK. The CBI is the UK member of UNICE, the European employers' federation.

As the CBI represents not only issuers but also law firms and financial institutions, many members also have submitted their own or contributed to the responses of LIBA, the BBA and the Law Society of England and Wales. Rather than duplicate the answers given elsewhere by others, we have concentrated on the main issues for our corporate members as issuers. As such, we have not responded to every single question but only to those of the greatest importance to our corporate members as users of the financial markets.

We note that some issues have not been covered in the consultation due to changes in the text of the Directive and would urge that there should be a further opportunity to consult on these in due course.

Certainty for issuers

It is important to state that not all issuers will be familiar with financial services legislation and their familiarity in dealing with the markets may vary considerably depending on their size and corporate activity. It is therefore important that the rules and guidance should be easy to comprehend to non-experts. In this respect, some of the draft guidance seems too detailed for Level 2.

The CBI believes that it is important that legitimate market practices should not be caught unexpectedly. The guidance should focus on whether or not information is price sensitive and whether or not it is material. Some of the wording is misleading - confidential information is not necessarily the same as inside information; not all confidential information will be inside information and not all inside information will be confidential.

CBI members have experience of the FSA's market abuse regime, which includes an element of intent in the concept of the "regular user" which has helped companies to understand better what is expected of them. This element of intent is implicit or, in some cases, explicit in the prohibitions in Articles 2 to 5 of the directive and in the definition of market manipulation. Therefore we would expect to see some reference to intent by CESR in its advice.

While from the regulators' viewpoint, flexibility may be helpful, this has to be balanced with the need for measures at Level 2 to be proportionate under Recital 43. Companies will approach this from the opposite point of view to the regulators – they will want certainty if they are to understand and then comply with the rules. Furthermore, we consider certainty to be essential for compliance with the European Convention on Human Rights because of the criminal nature of the provisions in the directive.

What would not be helpful to our members are very general rules without practical FAQs / examples, since otherwise the guidance will only need to be rewritten for companies by their lawyers, who may reach different conclusions among themselves as to what is required. **Practical examples written in plain language are what companies need.**

The FSA's Code of Market Conduct, for example, is written as guidance rather than rules in language aimed at companies as users of the financial markets. This approach is helpful. We appreciate that providing such examples will be time consuming and difficult under the current timetable but would urge that **this is the only way to provide guidance which will be easily understood and therefore effective.**

Discussions with others

While this should not be an excuse for market abuse, companies do need to have discussions with regulatory agencies, their advisers, major shareholders and others from time to time to take soundings as to possible courses of action. Regular discussions with shareholders are one of the aspects of good corporate governance. It is important that the regulatory regime encourages this, while providing that, if a company decided to discuss matters constituting inside information with shareholders, the company should obtain the agreement of such persons (a) not to take advantage of the information and (b) to be subject to a duty of

confidentiality. CESR's proposed guidance on Articles 6(1) and (2) needs to be looked at again in this light.

Other directives

As stated above, companies need to be clear as to what their obligations are. We note that there are several possible sources of rules for issuers as to what they should disclose in the form of the insider dealing & market manipulation, prospectus and transparency directives. This is likely to lead to confusion unless the directives and guidance are drafted in a joined up way, but so far this does not appear to have been the case. We would urge CESR to ensure that its work on the directives is carried out with clear lines of communication between the different working groups.

In addition, takeover rules should be dealt with separately and should not be subject to several different regulatory regimes. Thus Article 6(5) does not and, in our view, should not cover recommendations made in a takeover situation. Delay in the disclosure of information at an early stage of discussions about a takeover should also be covered by a safe harbour, provided that the disclosure follows rules set by the local regulatory authority.

As a matter of principle, we do not believe that CESR in its recommendations for Level 2 should amend primary legislation on company law e.g. re buyback provisions. Rather, if CESR has such views, it could make recommendations to the Commission or the High Level Expert Group on Company Law in order to avoid duplication. We do not consider that CESR should be trying to address issues of company law or corporate governance here but rather the integrity of the markets in the context of market abuse only.

Finally, the other major concerns for issuers are:

- the timing of announcements, which need to be meaningful
- the need for proper knowledge on the part of the issuer – all the necessary facts should have reached the relevant individual, rather than imputing to everyone knowledge within the organisation, which does not allow for e.g. Chinese walls - and
- the need for competition among disseminators of information to ensure innovation and the best service for both companies and investors.

We attach some additional thoughts on specific questions in the consultation paper and would be happy to provide further information on any of those or the above if this would be helpful.

Yours sincerely

Susannah Haan
Legal Adviser

Specific CBI comments

in response to CESR's consultation on market abuse

Inside information:

Commodity markets

We would urge CESR to learn from the FSA's experience of regulating such markets, by making requirements specific to the information, which the market would expect to receive. This would avoid adding unnecessary costs, which might cause such markets to move outside the EU. CESR should avoid a "one size fits all" approach and we believe that much of this could be left to Level 3.

Question 3 (p 13): Should the investor mentioned in the level 2 advice be qualified as reasonable / professional / informed?

The suggestion is that "A piece of information is likely to have a significant effect on the price of a financial instrument when it is information, which an investor could not omit to take into account or into consideration for his investment strategy."

We suggest that the text should read: "A piece of information... which a reasonable investor would be expected to take...". What is reasonable will depend upon the individual circumstances.

Although markets should receive information promptly, regulators should encourage the dissemination of meaningful information, a point highlighted by the Law Society response. Incomplete information may be misleading and sometimes holding announcements may be necessary.

Question 15: Are there any other relevant factors that should have been included?

CESR has set out a list on page 15 (paragraphs 46-50) of what it considers to be inside information, including matters such as changes in management, auditors, mergers, legal disputes, new licences or products, customer orders.

We believe that this list is potentially misleading and should not be treated as comprehensive; further, those matters which it does cover should not in themselves be inside information unless they pass other tests such as materiality and price sensitivity. We would prefer CESR to adopt the alternative wording provided by the British Banking Association on page 9 of their second response to CESR dated 26 September 2002.

Market manipulation:

If companies are to be able to comply with the rules, they need to be clear as to what is required of them. Worked examples including the necessary state of mind of what does or

does not constitute market manipulation and what “ought to have known” means would be helpful. CESR should also clarify that disclosure made to meet regulatory requirements will fall within a safe harbour and will not be misleading.

We do not see the diagnostic flags as being appropriate to Level 2; in fact we think that these would be confusing to most issuers. These are insufficiently focussed and would be better left to Level 3.

Question 10 (p 24): Factors to be taken into account at Level 2. Are there any additional factors to those on page 24?

We are concerned that these provisions should not cause difficulty to anyone choosing to sell a company’s shares in several blocks rather than all at once as that could have an adverse effect on a company’s share price. Sensible trading strategies should not be treated as market manipulation.

Article 6(1):

As stated above, it is important that it is clear to companies when information may be inside information in order that they may ensure compliance and in order to avoid confusion. It is also important that the question of timing of disclosures be made clear; “as soon as possible” should mean without undue delay.

Question 12 (p 27): CESR would be interested in receiving views on the disclosure obligations when a financial instrument is traded in more than one EU jurisdiction. The objective is to ensure equal treatment of all investors. For instance should an issuer be able to rely on disclosure through an officially appointed mechanism in one jurisdiction even when the instrument is traded in other jurisdictions as well?

In principle, information should be disclosed to all markets on which a company is listed. However, companies may not be aware of all the jurisdictions in which their instruments are traded and so should not be held responsible for disclosure in those jurisdictions over which the company had no choice as to whether its instruments were traded. Consideration needs to be given to the hours in which a company’s main market is open for business and the possibility of publication having to be out of hours - this may not be met with approval by the authority. Consideration should be given to a mechanism to allow for delay in the publication of information until companies’ main trading market is open.

We support the wording provided by the BBA on page 15 of their response.

Question 13 (p 28): CESR would welcome views on whether the EU needs a fully harmonised officially appointed mechanism. In putting forward any position, respondents are asked to articulate the costs and benefits of any proposal.

The CBI believes that a single body operating a monopoly would not be helpful. Competition will be the best means of ensuring accurate, up to date and efficient disclosure to the market.

The UK has several regulatory news services which ensures better focus on companies' needs. A single body would not have the same incentive to be customer focussed. It will also be important to ensure that there is an out of hours service such as exists in the UK, where the system works well.

We believe that competition between providers is the best means of ensuring that costs are kept low and that innovation takes place. The Regulatory News Service as former monopoly provider in the UK has become more responsive to companies' needs and more flexible in providing information and assistance, particularly out of hours, since the introduction of competition. This is in the long term interests of everyone; investors, companies and information providers alike. We therefore believe that CESR should encourage the dissemination of news by commercial providers such as Reuters, which have multi-jurisdictional reach and can ensure simultaneous access to information for investors.

Question 14 (p 28): Should there be technical implementing measures at Level 2 further defining the qualitative requirements “complete”, “prompt” and “not misleading”?

No. We agree that delay be allowed in the disclosure of information in certain circumstances, e.g. where a company is still to obtain patent approval, or is in discussions with existing shareholders, or for takeover discussions at an early stage. We support the wording provided by the BBA in response to Question 16 regarding prompt disclosure on page 17 of their response.

Question 15 (p 31): Would a definition of legitimate interests be useful as a Level 2 implementing measure? If yes, what definition would you propose?

No, we believe that this would be better left to Level 3.

Article 6(4) Research:

Many of our members have contributed to and therefore support the paper by the British Banking Association on research. The main points to note are that:

- ❖ companies' communications to their own shareholders and takeovers do not in our view fall within Article 6(5). If CESR disagrees, it should ask the European institutions to ensure that they are clearly excluded from the provisions of the Directive
- ❖ Chinese walls should be clearly recognised as a means of managing conflicts and should be taken into account in determining the appropriate level of disclosure and
- ❖ firms complying with US rules should be deemed to be in compliance with EU standards.

Article 8 Safe Harbours (p 43):

The Directive establishes a safe harbour for buybacks. However, CESR seems to be trying to remove existing safe harbours under company law and adding to reporting requirements.

Since in the UK the shareholders will have approved the buyback we consider such restrictions to be unnecessary. We also believe that debt buybacks should be allowed under the safe harbour, since it may be in a company's interests to redeem its debt in advance of the due date. This will usually be in accordance with the contractual agreement and should be recognised as a safe harbour activity.

It should also be made clear that the fact that a particular activity does not fall within a safe harbour does not necessarily make it market abuse.

Trading in own shares under a “buy-back” programme (p 44):

Question 30: Are these measures appropriate to mitigate insider dealing risks?

The measures seem to be excessive. CESR's recommendations should not change company law and remove the existing safe harbour for companies to buy back their own shares.

Share buybacks should be permitted under the safe harbour but should not need to be formally announced or for special disclosure to be given in advance. Where buybacks are undertaken in accordance with contractual agreements or by way of prior shareholder approval, they should fall within the safe harbour.

Sale of own shares (p 45-46):

CESR proposes to remove the safe harbour for sale of own shares during the period of the buy-back programme. We disagree with this proposal. Sales should be looked at on their merits and should not impact the availability of the safe harbour.

Question 31: Does this achieve an appropriate balance with regard to the EU's regulatory objectives (particularly as between the objectives of market integrity and efficient allocation of capital)? How could CESR introduce more flexibility in this area?

If an acquisition opportunity were to arise during a buyback period, this should not be prevented by removing the safe harbour. Perhaps some mechanism could be found to allow more flexibility, e.g. by suspending the buyback or obtaining shareholder permission.

Question 32: Should CESR introduce a time limit of less than 18 months (amending the Second Company Law Directive authorising buybacks within 18 months)?

CESR should not itself change company law; if it has recommendations, these should be passed to the High Level Expert Group looking at EU company law and corporate governance. 18 months allows for the gap between AGMs being more than 12 months, as can happen if a company has changed its accounting period.

Question 34: Should off-market transactions be disallowed for the purposes of the safe harbour?

No. These should be allowed.

Question 35: Should companies be restricted from buying more than 25% of the average daily volume?

No.

Question 36: Should the Competent Authority be given such a power (to suspend a buyback programme)?

Yes, although the power should only be used in extreme circumstances.