ESMA CONSULTATION PAPER 1016/162 – DRAFT GUIDELINES ON THE MARKET ABUSE REGULATION

Law Society and City of London Law Society
Company Law Committees Joint Market Abuse Working Party Response

Introduction

The comments set out in this paper have been prepared jointly by the Market Abuse Joint Working Party of the Company Law Committees of the Law Society of England and Wales (the "**Law Society**") and the City of London Law Society ("**CLLS**").

The Law Society is the professional body for solicitors in England and Wales, representing over 160,000 registered legal practitioners. It represents the profession to Parliament, Government and regulatory bodies in both the domestic and European arena and has a public interest in the reform of the law.

The CLLS represents approximately 15,000 City lawyers through individual and corporate membership, including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multijurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

The Market Abuse Joint Working Party is made up of senior and specialist corporate lawyers from both the Law Society and the CLLS who have a particular focus on issues relating to capital markets.

GUIDELINES FOR PERSONS RECEIVING MARKET SOUNDINGS

General

Before noting our views in respect of those questions on which we have comments, we would like to make the following general comments:

(a) **Proportionality**

Whilst we understand a desire to draft the guidelines for MSRs in a similar style to the rules for DMPs, we are concerned that, whilst DMPs will be authorised/regulated firms which will already have in place compliance teams and systems in order to comply with regulations applicable to them or issuers (which are likely to rely on intermediaries for much of the compliance procedures), MSRs may comprise investors for whom receiving a market sounding may be incidental to their primary business and who may not otherwise have compliance functions in their organisations or related systems and procedures. Furthermore, such MSRs may not have the resources to put in place the level of compliance procedures required by the guidelines.

We are, therefore, concerned that the guidelines for MSRs will not always be proportionate. This could also create an unequal playing field with markets in non-EU jurisdictions which do not impose such a prescriptive regime.

Whilst we appreciate that it would be possible for an MSR who is in this position to advise the DMP that it does not wish to receive soundings, it does not seem right to us that MSRs should have to refuse to receive soundings for that reason.

MSRs that do not have compliance functions and, in particular, those based outside the EU, may not be aware of the guidelines for MSRs and we wonder if it would be a good idea for DMPs to have to make MSRs aware of the guidelines before providing a sounding.

(b) **Extra-territorial reach**

It is not clear to us how the guidelines would apply to a market participant who is outside the EEA.

Q1: Do you agree with this proposal regarding MSR's assessment as to whether they are in possession of inside information as a result of the market sounding and as to when they cease to be in possession of inside information?

The proposal seems sensible but there does not appear to be any recognition that some information that may be relevant to the assessment might sit behind a Chinese Wall within an MSR and it would be helpful for there to be clarity as to whether an MSR is required to take such information into account.

Q2: Do you agree with this proposal regarding discrepancies of opinion between DMP and MSR?

We agree.

Q3: Do you agree with this proposal regarding internal procedures and staff training? Should the Guidelines be more detailed and specific about the internal procedures to prevent the circulation of inside information?

As explained above, not all MSRs will be regulated entities: they may be individuals or companies that are not listed and may not be based in the EU. They may only receive market soundings very infrequently. We therefore think that the proposal regarding internal procedures and training will impose too great a burden on many MSRs. Furthermore, we question whether the requirement for MSRs to train their staff goes further than Article 11 of MAR envisages, in that the Article only refers to ESMA issuing guidelines regarding the steps that MSRs are to take in order to comply with Articles 8 and 10.

We do not, in any case, think that the guidelines should be more detailed or specific.

Q4: Do you agree with this proposal regarding a list of MSR's staff that are in possession of the information communicated in the course of the market sounding?

We wonder if the guidance could be clearer on this point. We do not think that it is immediately clear what "in possession of" means. Does it mean that persons who have substantive or active involvement with the sounding are "in possession of it" or is a more passive recipient in possession e.g. someone who manages e-mail or post for another.

Also, what does the term "working for" mean? Does it extend to professional advisers? We think that this should be restricted to staff of the MSR. Again, we question the proportionality of this requirement seeing that many MSRs may not have the internal systems to comply with these requirements.

As drafted, the rules would have to be applied in the same way to every situation which would not always be appropriate or proportionate. In particular, we note that the guidance relates to all information that is communicated in the course of a market sounding and does not relate only to soundings which include inside information. We do not think it is appropriate to impose a burden of compliance in situations where no inside information is imparted.

Q5: Do you agree with the revised approach regarding the recording of the telephone calls?

The revised approach seems sensible. Where, as will normally be the case, there is more than one DMP involved in a market sounding call we note that the MSR will have to sign more than one record of the call, which we do not think is proportionate.

Q6: Do you agree with the proposal regarding MSR's obligation to draw up their own version of the written minutes or notes in case of disagreement with the content of those drafted by the DMP?

We think that the wording of Article 6(2) of the Delegated Regulation and Guidance note 8(b) do not work particularly well together. The Delegated Regulation wording seems to mean that the DMP and MSR have five working days to reach agreement but the guidance, read on its own, suggests that the MSR should provide its own minutes within five working days of the sounding if it does not agree with the DMP's version, but provides no time by which the DMP must provide its version to the MSR. If the MSR did not receive the DMPs version until the fifth working day after the sounding, and did not agree with it, the MSR may find that it cannot comply with this obligation. We have attempted to cover this issue in the attached copy of the guidelines which includes some suggested changes.

GUIDELINES ON LEGITIMATE INTERESTS OF ISSUERS TO DELAY INSIDE INFORMATION AND SITUATIONS IN WHICH THE DELAY OF DISCLOSURE IS LIKELY TO MISLEAD THE PUBLIC

Q8: Do you agree with the proposal regarding legitimate interests of the issuer for delaying disclosure of inside information?

Preparation of results

We consider that there needs to be clarity that the process of preparing results (annual and interim) for publication does not trigger a requirement for disclosure of inside information before the planned date for the publication of the results (except where it is clear that the results to be published are so divergent from expectations that a disclosure amounting to a profit warning is required). Under the existing UK regime it has been the general practice (acceptable both to regulators and market participants) for issuers to publish results in accordance with a planned (and usually disclosed) timetable (except where a profit warning is required). We think it is important that issuers should understand that this practice is acceptable and the circumstances in which accelerated disclosure is required. Paragraph 64 of the consultation does not provide the clarity that is required.

It would be helpful if ESMA would clarify how it believes issuers should analyse the question. We see a number of possible explanations for the issuer's ability to keep to its planned results timetable (absent exceptional circumstances):

(a) results which are in line with market expectations should generally be regarded as not giving rise to inside information; or

(b) the delay in publishing the results would nonetheless be consistent with the requirement to publish "as soon as possible"; or

(c) there is no inside information until the results have been approved by the board (on the basis that the information may not be considered to be precise till this stage); or

(d) the issuer is entitled to rely on the ability to delay on the basis that accelerated disclosure would prejudice its legitimate interest in maintaining an orderly reporting process.

If the explanation in (a) is correct there will be no market abuse if dealings take place during the process of results preparation. If any of the other explanations applies it becomes necessary for issuers to identify the moment in time when the information it has is inside information. This is likely to be problematic and it would avoid this potentially challenging analysis if it is acceptable for issuers to identify the commencement of the results preparation process as the point in time when information has or may have come into existence.

Unexpected and significant events

We understand paragraph 67 of the consultation to mean that, where an issuer is faced with an unexpected and significant event, it may need some time to clarify the situation and that this does not involve exercise of the right to delay but that the requirement under Article 17(1) to inform the public “as soon as possible” allows the issuer time to obtain clarification so that it can make a useful and reliable disclosure. It would be useful if ESMA could confirm this is correct.

Buying or selling a major holding in another entity

As regards paragraph 1(e) of the draft Guidelines, which paragraph 86 of the consultation paper explains relates to planning the acquisition or disposal of shares where negotiations have not yet started, we do not understand why planning this particular kind of transaction is singled out. We consider that there should be a more general ability to delay disclosure of the planning stages of other kinds of transactions/corporate developments where negotiations may not have started. Also, we think the test "would jeopardise" is too strict. An issuer will have to make the judgment as to whether disclosure of information is likely to jeopardise the conclusion of a transaction without knowing what the reaction of the other parties involved would be. We think the test should be "is likely to jeopardise or adversely affect" (which is the wording used in Guideline 1(d)).

Resignation of CEO

We are unsure why ESMA consider that the case of a CEO resigning will not amount to a legitimate interest (paragraph 63 of the consultation paper). We believe that there are circumstances where it would be legitimate for an issuer to delay such a disclosure, particularly, for example, where the resignation is not with immediate effect in order to allow time to find a suitable replacement.

Approach to interpreting the right to delay

We note the comment in paragraph 69 of the consultation that the possibility to delay disclosure should be narrowly interpreted. We do not agree but think the SMSG was correct in its contrary view. The ability to delay disclosure is an important balance to the broad scope of the definition of “inside information”. On the one hand the policy of the regulation is to restrict dealings where there is information which provides an unfair advantage, which tends to a broad view of what is inside information. On the other hand, issuers have a considerable burden for making disclosures if all inside information must be disclosed even where to do so would damage the issuer (to the disadvantage of all its stakeholders). That would tend to a narrower scope for

inside information. The ability to delay provides a way to bridge this gap – allowing a broad view of inside information but avoiding too many damaging disclosures.

Q9: Do you agree with the proposal regarding situations where the delayed disclosure is likely to mislead the public?

We consider that the approach in the Guidelines to the question of when a delay would be misleading is stated too definitively, in particular, in paragraphs 2(b) and (c) of the draft Guidelines (and paragraphs 100 and 102 of the consultation paper). We suggest that all of the issuer's disclosures of its financial objectives should be taken into account to determine whether a subsequent divergence is misleading (for example, a forecast accompanied by appropriate disclosure of assumptions/risks to achievement would not be misleading if a subsequent divergence was due to one of those assumptions not being met). It may be only on rare occasions that there will be a legitimate interest to be protected by a delay of such a disclosure but it would be wrong to rule out that possibility where the previous disclosure was such that investors cannot be said to be misled by the delay.

Drafting

As noted above, there are aspects of the draft guidelines which we think could be expressed more clearly and in other cases we consider that the terms impose a more restrictive approach than seems to us to be justified. (For example Recital (50) of MAR specifically states that legitimate interests may relate to ongoing negotiations, or related elements, where the outcome or normal pattern of those negotiations would be likely to be **affected** by public disclosure, so we do not think that ESMA should impose a more onerous requirement, as it is seeking to do in the suggested drafting of 1a in the Proposal of Guidelines.) We include in the Appendix a copy of the draft guidelines in which we have marked some suggested changes to the text.

We should be happy to discuss the points made in this paper or the drafting of the guidelines with ESMA.

31 March 2016

Appendix

2.12 Proposal of guidelines

1. Designated persons or contact point within the MSR entitled to receive market soundings

Where ~~the~~a person receiving ~~the~~a market sounding (MSR) designates a specific person or a contact point to receive the market sounding, the MSR should take reasonable steps to ensure that that information is made available to ~~the~~ disclosing market participants (DMP).

2. Communicating the wish not to receive market soundings

~~After~~Upon being ~~addressed~~contacted by a DMP~~,~~ for the purposes of a market sounding, a MSR should notify ~~it whether~~the DMP if they do not wish ~~not~~ to receive ~~future~~ market soundings on any occasion or in relation to ~~either all potential transactions or~~ particular types of potential transactions.

3. MSR's assessment as to whether they are in possession of inside information as a result of the market sounding and as to when they cease to be in possession of inside information

1) While taking into account the DMP's assessment~~, MSRs~~ of whether it is reporting inside information to the MSR, the MSR should independently assess whether they are in possession of inside information as a result of the market sounding, taking into consideration as a relevant factor all the information ~~available to~~held by them, including the information obtained from sources other than the DMP.

2) While taking into account ~~the~~a DMP's notification that the information disclosed in the course of the market sounding is no longer inside information, ~~MSRs~~the MSR should independently assess whether they are still in possession of inside information, taking into consideration all the information ~~available to~~held by them, including the information obtained from other sources than the DMP.

4. Discrepancies of opinion between DMP and MSR

1) In the case of market soundings where, according to the DMP, no inside information is disclosed, where the MSR assesses on the contrary that they are in possession of inside information they should:

   a. refrain from informing the DMP of the discrepancy of opinion if the different assessment is due to the fact that the MSR is in possession of other information than that received from the DMP; or

   b. inform the DMP of the discrepancy of opinion if the different assessment is based exclusively upon the information that the MSR received from the DMP.

2) In the case of market soundings where, according to the DMP, inside information has been disclosed, where the MSR receives the DMP's notification informing the MSR that the

information communicated in the course of the market sounding has ceased to be inside information and disagrees with the DMP's conclusion, the MSR should:

a. refrain from informing the DMP of the discrepancy of opinion if the different assessment is due to the fact that the MSR is in possession of other information than that received from the DMP; or

b. inform the DMP of the discrepancy of opinion if the different assessment is based exclusively upon the information that the MSR received from the DMP.

5. Internal procedures and staff training

1) The MSR should establish, implement and maintain internal procedures to:

a. ensure that the information received in the course of ~~the~~a market sounding is internally communicated only through pre-determined reporting lines and on a need-to-know basis;

b. ensure that the function or body entrusted to assess whether the MSR is in possession of inside information as a result of the market sounding ~~are~~is clearly identified and is composed of staff properly trained ~~to~~for that purpose;

c. manage and control the flow of inside information arising from the market sounding within the MSR and its staff, in order for the MSR and its staff to comply with Articles 8 and 10 of MAR.

2) The MSR should ensure that the staff receiving and processing ~~the~~ information provided in the course of ~~the~~a market sounding are properly trained on the relevant internal procedures and on the prohibitions, under Articles 8 and 10 of MAR, arising from being in possession of inside information.

6. List of MSR's staff that are in possession of the information communicated in the course of the market soundings

For each market sounding, MSRs should draw up a list of ~~the persons working for them that~~their staff who are in possession of the information communicated in the course of the market ~~soundings~~sounding.

7. ~~Assessment~~Identification of related issuers and financial instruments

Where the MSR has assessed that they are in possession of inside information as a result of a market sounding, the MSR should identify all the issuers and financial instruments to which that inside information relates.

8. Written minutes or notes

Where in accordance with [Article 6(2)(d) of Delegated Regulation (EU) .../...[RTS on Market soundings]] the DMP has drawn up written minutes or notes of ~~the~~an unrecorded ~~meetings~~meeting or unrecorded telephone conversation~~, the MSRs~~ with a MSR and has provided a copy to the MSR, the MSR should:

a. sign the copy of these minutes or notes where they agree ~~upon~~with their content; or

b. provide the DMP with their own version of the minutes or notes duly signed within five working days after ~~the market sounding~~receipt of the MSR's minutes or notes where they do not agree ~~upon~~with the content of the minutes or notes drawn up by the DMP.

9. Record keeping

MSRs should keep records in a durable medium that ensures accessibility and readability for a period of five years of:

a. the notifications referred to in paragraph 2;

b. the assessments referred to in paragraph 3 and the reasons therefor;

c. the discrepancy of opinion referred to in paragraph 4;

d. the procedures referred to in paragraph 5;

e. the lists referred to in paragraph 6; and

f. the ~~assessment of related~~identification of issuers and financial instruments referred to in paragraph 7.

3.4 Proposal of guidelines

1. Legitimate interests of the issuer for delaying disclosure of inside information

For the purposes of point (a) of Article 17(4) of Regulation (EU) No 596/2014, the cases where immediate disclosure of the inside information is likely to prejudice the issuers' legitimate interests could include but are not limited to the following circumstances:

a. the issuer is conducting negotiations, where the outcome or normal pattern of such negotiations would be likely ~~be jeopardised~~to be adversely affected by immediate public disclosure of that information;

b. the financial viability of the issuer is in grave and imminent danger, although not within the scope of the applicable insolvency law, and immediate public disclosure of the inside information would seriously prejudice the interests of existing and potential shareholders~~, jeopardising~~ by adversely affecting the conclusion of the negotiations aimed at ensuring the financial recovery of the issuer;

c. the inside information relates to decisions taken or contracts entered into by the management body of an issuer which need, pursuant to national law or the issuer's bylaws, the approval of another body of the issuer, other than the shareholders' general assembly, ~~of the issuer~~ in order to become effective, provided that all the following conditions are met:

i. immediate public disclosure of that information before such ~~a definitive~~ approval would jeopardise the correct assessment of the information by the public;

ii. an announcement explaining that such approval is still pending would jeopardise the freedom of decision of the other body;

iii. the issuer arranged for the decision of the body responsible for such approval to be made, ~~possibly, within~~in so far as reasonably practicable, on the same day as the decision taken or contract entered into by the management body; and

iv. it cannot reasonably be expected that the decision of the body responsible for such approval ~~is not expected to be in line with~~will necessarily follow the decision of the management body, as for instance it would be where [the majority of] members of such body ~~is the expression of the same shareholders represented in~~and the management body ~~or in cases~~are representatives of the same particular shareholders or where such body has consistently approved the management body's decisions on similar issues.

d. the issuer has developed a product or an invention and the immediate public disclosure of that information is likely to jeopardise the intellectual property rights of the issuer;

e. the issuer is planning to buy or sell a major holding in another entity and the disclosure of such ~~an~~ information ~~would~~is likely to jeopardise ~~the conclusion of the transaction~~or adversely affect the implementation of such plan;

f. a transaction previously announced is subject to a public authority's approval, and such approval is conditional upon additional requirements, where the immediate disclosure of those requirements will likely affect the ability ~~for~~of the issuer to meet them or to affect adversely the issuer's ability to negotiate the requirements with that or any other relevant public authority in the issuer's interests and therefore ~~prevent~~prejudice the ~~final~~likely success of the ~~deal or~~ transaction.

2. Situations in which delay of disclosure of inside information is likely to mislead the public

For the purposes of point (b) of Article 17(4) of Regulation (EU) No 596/2014, the situations in which delay of disclosure of inside information is likely to mislead the public ~~includes~~include at least the following circumstances:

a. the inside information whose disclosure the issuer intends to delay is materially different from a previous public announcement of the issuer on the matter to which the inside information refers ~~to~~;

b. [the inside information whose disclosure the issuer intends to delay ~~regards~~is the fact that the issuer's financial objectives, as disclosed by all relevant prior announcements of the issuer relating thereto, are likely not to be met, ~~where such objectives were previously publicly announced~~in a material respect;]

c. [the inside information whose disclosure the issuer intends to delay is ~~in contrast with~~ the ~~market~~fact that the issuer's expectations~~, where such~~ of its financial results are materially different from the expectations of investors generally, where such investors' expectations ~~are based on signals that~~have arisen from information the issuer has previously ~~set.~~provided and investors would reasonably expect that information to be updated.]