THE COMMITTEE OF EUROPEAN SECURITIES REGULATORS

Ref.: CESR/03-213b

Additional Level 2 Implementing Measures for

Market Abuse Directive

FEEDBACK STATEMENT

August 2003

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Introduction

1. On 27 March 2002, the European Commission mandated CESR to provide technical advice on possible implementing measures for aspects of the Directive on Insider Dealing and Market Manipulation (Market Abuse) which it did on 31 December 2002: "CESR's Advice on Level 2 Implementing Measures for the proposed Market Abuse Directive" [Ref: CESR/02.089d).

2. On 31 January 2003, the Commission published "An additional mandate to CESR for technical advice on possible implementing measures concerning the Directive on Insider Dealing and Market Manipulation (Market Abuse)" (Ref: MARKT/G2 D (2003). CESR submitted its advice on 31 August 2003.

3. This feedback statement will discuss the main points which were made by respondents in the consultation process on CESR's advice and explain the policy options which CESR decided upon.

4. Five substantive areas were covered in the Commission's Additional Mandate to CESR. These were:
   - Guidelines for Determining Accepted Market Practices
   - Definition of "Inside Information" for Derivatives on Commodities
   - Lists of Persons having access to Inside Information
   - Disclosure of Transactions
   - Suspicious Transactions

5. CESR undertook a number of steps prior to the submission of its advice to the Commission:

6. CESR's Expert Group on Market Abuse, chaired by Pr. Stavros Thomadakis, Chairman of the Hellenic Capital Market Commission and supported by Mr Nigel Phipps of the CESR secretariat, was responsible for the work on the second set of advice to the Commission, as it was for the first set.

7. CESR's Expert group was aided in this task by the outcome of the Call for Evidence (Ref: CESR/03-037), which closed on 28 February 2003. This invited all interested parties to submit their views on what the content of CESR's advice to the Commission should be. The 20 responses received can be viewed on CESR's website.

8. CESR's Expert group was also assisted by the Consultative Working Group (CWG) which was composed of a broad cross-section of EU market experts. In addition, representatives of Europe's commodities markets, and of the US CFTC, provided valuable guidance for CESR's work on the definition of inside information for derivatives on commodities.

9. In April 2003 CESR published a Consultation Paper, "Market Abuse: Additional Level 2 Implementing Measures" [Ref: CESR/03-102b) which set out its proposals for technical implementing measures in the areas identified in the Mandate and requested comments on particular questions posed. The closing date for consultation responses was June 15, 2003. A public hearing was held in Paris on 12 May 2003, and there were also a number of bilateral meetings and national consultative events.

10. Over 70 responses were received in response to the consultation. These came from a variety of sources including individual banks, investment services firms, asset managers, regulated markets and exchanges, trade associations and financial analysts and rating agencies. Issuers

were particularly well represented. Five responses were received from European federations. All public responses can be viewed on the CESR website.

11. This feedback statement will focus on the substantive points which were raised in each of the five technical areas in which CESR was requested to provide advice. In each area the feedback statement will focus on the key issues. These will be followed by a combination of subsidiary points and answers to the questions posed in the consultation paper.

12. The majority of responses supported the overall approach adopted by CESR in its proposals. This was a focus on high level principles and the procedures for determining accepted market practices (AMPs) rather than an attempt to define detailed lists of particular practices. The key issue that emerged from the feedback was the appropriate degree of harmonisation that should be sought at level 2 or level 3. It was accepted that harmonisation and convergence of views on particular practices was desirable, but it was also recognised that there would be occasions when the same practice would be regarded as acceptable by one competent authority and not by another. Detailed discussions on particular practices should therefore be left to level 3 rather than level 2.

13. Respondents were keen to stress that there should not be a universal list of acceptable market practices. CESR agrees with this and has added a sentence to this effect in the explanatory text of the advice (new paragraph 2).

14. Concerns were expressed about the implications of having specific practices endorsed as "acceptable" since it would be impossible to consider every conceivable type of market practice. Would practices where a view had not been published by a competent authority be regarded as unacceptable? How would market participants be sure that normal business practices would not be deemed to be unacceptable? As outlined in the explanatory text, the concept of an AMP is only relevant when a particular practice appears to fall within the Directive's definition of market manipulation and many everyday business practices would not fit within this. In addition, as the advice notes, the fact that a view has not been expressed on a particular practice should not be interpreted as meaning the practice is unacceptable since this would hinder innovation and create uncertainty.

Other points

15. There was a need to establish that, just because a practice was acceptable or unacceptable in one EU country, this should not be taken to mean it was also the case in every EU country. Paragraph 35 bullet point 5 has been amended to establish this. Convergence is encouraged but there is also a recognition that justifiable differences of opinion may remain. When publishing views on a particular practice, competent authorities should pay particular attention to explaining any differences of view regarding the acceptability of a practice amongst CESR members.

16. A number of responses questioned the factor concerning the impact that the prevalence of a practice should have on its acceptability. A practice that was widespread might indicate broad acceptance, but the corollary was not necessarily true, since a new or innovative practice would, by definition, not be commonplace, but should not automatically be deemed to be unacceptable. Conversely, it may not necessarily follow that a widespread practice, particularly one that has developed rapidly, will be deemed to be acceptable. This 'prevalence' factor has been deleted from the advice therefore but the explanatory text has been revised to communicate that this is still a relevant factor for consideration.

17. The consensus, although not the unanimous opinion, was that CESR's advice should reflect the differences between OTC and regulated markets. The advice now does this; for example the factor which requires consideration of the market's structural characteristics now explicitly refers to whether it is an OTC or a regulated market. It was also felt that the comment that increased transparency and liquidity meant a transaction was more likely to be acceptable was potentially misleading when read in the context of OTC markets. A new sentence in the advice

now states: "…practices on OTC markets are less transparent than on regulated markets but this does not mean that such practices are automatically less acceptable".

18. Respondents felt that the reason or motivation for an activity should be taken into account in determining whether or not it was an acceptable market practice. According to the Directive, where "certain practices appear to meet the definitions of market manipulation set out in Article 1(2) (a), they may nevertheless not amount to market abuse where the person concerned establishes that his reasons were legitimate and the transactions or orders to trade conform to accepted market practices on the regulated market concerned." In CESR's opinion, the motivation for an activity is not a defence against an accusation of market manipulation though the text of the Directive itself does include some element of motivation in the test when it speaks of "legitimate reasons".

19. In response to the request that appropriate descriptions be provided to aid transparency, CESR has incorporated an additional sentence in original paragraph 36, bullet point 2. This states that a description of the factors used to determine the acceptability of a practice should be published, particularly where the competent authority's decision differs from another EU regulator.

20. The comment that codes of conduct are of lower regulatory status compared to rules or regulations has been removed in response to example of codes that have been drawn up in accordance with statutory requirements in some jurisdictions and which carry significant evidential weight.

21. It was stressed that even market practices listed as acceptable may, over time, become unacceptable, perhaps because of changes to the relevant market's characteristics. The new bullet point 4 in paragraph 14 explains that the procedures for establishing acceptability should also be followed to review whether the acceptability of a practice changes.

22. Some respondents sought clarification about the scope of the concept of the "wider market". This has been changed to "directly or indirectly related markets", and "trading venue" has been altered to "exchange (or other trading venue)" to target the advice more accurately. Paragraph 35 bullet points 4 and 5 have therefore been modified. Some felt the original wording gave too much emphasis to other markets and that the focus should be on Europe and not AMPs elsewhere. CESR accepts this and therefore has added the phrase "within the EU" to paragraph 35, bullet point 4.

23. It was mentioned that the last sentence of paragraph 35, bullet point 2 was unclear and thus should be deleted. CESR disagrees with this, believing that its meaning is transparent and that the qualifier "less" makes it clear that it is not a proscription.

24. Certain banks suggested that an obligation should be placed on competent authorities to consult a wider spectrum of relevant parties before deciding whether a practice should be deemed acceptable or not. CESR has modified its advice in paragraph 36, bullet point 1 to clarify that all relevant market participants should be consulted. There is also now a requirement that "other competent authorities, including those in other jurisdictions where comparable markets exist, should also be consulted in order to reach a common position on the acceptability of practices".

Questions

Question 1: *Is the proposed approach appropriate, focusing both on the characteristics of particular market practices and the procedures that Competent Authorities should follow?*

25. The general tenor of responses was that CESR's approach was indeed appropriate.

26. CESR in its response to the consultation, and in its advice, has been mindful of this but it has also been concerned to avoid the possibility of regulatory arbitrage and conscious of the requirements of the level 2 mandate.

27. Two respondents felt that it would be useful to have a further sub-division of the factors involved. One suggestion was that the factors should be re-organised to prioritise them in terms of their importance to the market. CESR does not believe that these changes would be beneficial enough to merit a rearrangement of the factors.

Question 2: *Are the suggested principles, factors and procedures appropriate? Would you consider adding more factors such as the degree to which a practice has a significant effect on prices and in particular on reference prices?*

28. Many respondents felt that the extent of retail participation should not be of prime importance in the event of an investigation. CESR has not amended its advice in this area since the reference here is to the type of market participants and CESR believes that this is a relevant consideration.

Question 3: *The Directive focuses on accepted market practices "on the regulated market concerned", but the prohibitions of the Directive also apply to OTC trading. Is it necessary to make any distinction between standards of acceptable market practices on regulated markets and OTC practices? Is it also necessary to make distinctions between standards of acceptable market practices in different kind of regulated markets or MTFs (e.g. order driven or price driven)?*

29. Respondents were generally adamant that there should be a distinction in both cases since there were different requirements, rules and customs. Some respondents felt that the distinction was apparent in the consideration of the market's structural characteristics and thus already covered in the advice. Some did believe that there should be a consistent approach for both market types.

30. It was felt that AMPs for OTC instruments where the underlying was not a listed financial instrument should consider whether the practice conforms to relevant codes of conduct. CESR's advice would, where this was appropriate, allow this.

31. Although the definition of accepted market practices under paragraph 5 of article 1 of the Directive covers all financial markets, the AMP defence (paragraph 2 article1) is restricted to a practice carried out on a regulated market. It was felt that CESR should expressly extend this defence to someone carrying out practices in any financial market. CESR recognises that there is a lacuna here but this is not an area that can be addressed at level 2.

Question 4: *Do you agree that a practice need not be identifiable as already having been explicitly accepted by a competent authority before it can be undertaken?*
The consensus was that this should be a definite yes. One caveat was that the burden of proof should be placed on the competent authority. CESR does not agree and is of the view that market participants also bear responsibility for ensuring that their behaviour complies with the Directive.

Question 5: *CESR is committed to the future discussion of specific market practices as part of the Level 3 work necessary to increase the harmonisation of accepted practices where appropriate. Please specify any examples of particular practices which you consider could be classified as accepted market practices for the purposes of the Directive.*

32. Examples given were:
- Use of Volume Weighted Average Price (VWAP);
- The sale or repurchase of securities in the regulated market for the sole purpose of providing evidence of an official market price for illiquid securities;
- Pre-arranged post trading for options and their hedging;
- The practice of marking the close for orders executed on behalf of certain clients;
- Short selling;
- Matched orders;
- Position limits;
- Pre-arranged trades;
- Warehousing.
- The Danish mortgage banks' market making in less liquid mortgage bonds;

33. Respondents also gave examples of practices that were not acceptable:
- Intentional crossing by the same firm acting as principal;
- Spoofing (the deletion of "anomalous" orders during the final part of an auction);
- Entering transactions which were not intended to transfer the ownership of the financial instrument or change the participant's exposure to market risk.

34. CESR has not expressed any views, in either direction, on these examples.

Definition of "Inside Information" for Derivatives on Commodities

35. Respondents in general supported the approach that CESR had proposed in this area. They commented that the additional consultation that CESR had undertaken meant that there was a good appreciation in the advice of the special characteristics of commodity derivatives markets.

Key Issues

36. The key issue was the scope of information that would be "generally available", which was felt to be too wide and imprecise. Respondents were concerned that information would have to be published even if it had already been made available through other sources. This was not CESR's intention. CESR therefore has altered its advice in paragraph 46. The revised paragraph now captures information that has been *announced* or *disclosed* i.e. that no longer constitutes "inside" information.

37. The concept of disclosure therefore has been added to both the original paragraphs 46 (ii and iii) and 47 (ii), a refinement that was sought by respondents to add precision. For paragraph 47(ii) it replaces "published". The concept of disclosure, in accordance with certain requirements, is not as broad a concept as publication and the change is consistent with the tenor of the directive.

38. Some respondents argued that it was wrong to assert that market users "expected" information without a link to the efforts of the market user to obtain that information. CESR believes that the modifications to paragraphs 46 and 47 previously discussed clarify that it was not CESR's intention to leave a loophole whereby a user might claim it was unaware of an announcement. CESR's policy position has not changed.

Other Comments

39. Respondents felt that paragraph 46(i) was too broad. Some expressed doubt as to whether the advice, as worded, would provide a sufficient basis for prosecution. CESR therefore has inserted the phrase used in the Directive, namely "relating, directly or indirectly, to one or more commodity derivatives" to clarify this.

40. The word "generally" in paragraph 46 (i) has been replaced by the phrase "routinely made" to reinforce that what should be captured is information that is *expected* by market users to be available to them. It does not therefore cover all information which may relate to the underlying commodity.

41. Rather than maintain the original paragraph 46, bullet points (ii) and (iii), CESR has conflated them into a revised paragraph in the level 2 advice which retains the two sentences' intention to capture both "relevant commodity derivatives market" and the "relevant underlying commodity market". The comment was made that the guidance should emphasize that the definition of inside information does not include information which becomes public as a result of disclosure obligations which do not relate to the regulated market on which the relevant commodity derivative is traded. The revised advice now does this.

42. A number of respondents suggested that the "or" at the end of paragraph 46 of the level 2 advice should be replaced with an "and". The reason why this change was not incorporated was that the intention of paragraph 46 was to capture, for instance, government measures, indices and announcements (eg in relation to the US Strategic Petroleum Reserve) for which there is no disclosure requirement and thus which would not be captured by the other

subparagraphs of paragraph 46. The effect of changing the "or" to an "and" would be to say that users do not expect to receive information such as the US SPR. This, in CESR's view, would not be correct.

43. The proposal from respondents that "contracts" in paragraphs 46 and 47 should be expanded to "contract terms and specifications" has not been incorporated. The purpose of the original wording is to cover all disclosure "as a result of.... contracts"; if the matter falls to be disclosed under any term, condition or for any other reason under a contract, it should be disclosed. The longer and more precise wording proposed by respondents creates a risk that contract provisions may be characterized as neither terms nor specifications and hence no disclosure of information under those provisions is made. The original wording has therefore been retained.

44. The last sentence to paragraph 46 has been changed into a separate point in the advice. This refers to the revised advice on Accepted Market Practices regarding the procedures to be followed by competent authorities when considering whether to accept, or continue to accept, particular market practices.

45. Many respondents noted that it is unfortunate that neither a price sensitivity test, nor a materiality test, is included in the Level 1 definition of inside information on commodity derivatives markets. CESR cannot, however, propose amendments to Level 1 provisions with Level 2 advice.

Questions

Question 6: *Has CESR correctly identified all the relevant and material market, product and information factors relevant to the definition of "inside information" for commodity derivatives?*

46. One respondent inquired about the scope of CESR's approach, with specific regard to agricultural commodity derivatives; for example, whether politicians or vets were included in the list of potential holders of insider information. It is beyond the scope of CESR's mandate to draw up a definitive list of those captured by the Directive.

47. Respondents did not identify any additional factors relevant to the definition of inside information for commodity derivatives.

Question 7: *Is there further information which is material, relevant and disclosable in relation to commodity derivatives markets?*

48. More information was asked for on changes to contract characteristics, margin/collateral requirements, whether there was a temporary shortage in the underlying and on the underlying product for securitised commodity derivatives. Some investment services firms wanted the publication in each jurisdiction of disclosed information on the underlying. It was suggested that, for securitised commodity derivatives, information should be provided by brokers and market makers as well as the market operator.

49. CESR was concerned about advising the imposition of such burdens in EU law. The usefulness of such information might be outweighed by the dangers of excessive and inappropriate information.

Question 8: *Does the draft advice accurately reflect the information relating to underlying commodities which commodity derivatives markets users expect to receive?*

50. Respondents did not identify any inaccuracies in CESR's draft advice in this respect.

Question 9: *Is there any additional guidance that CESR should consider giving in relation to the definition of "inside information" for commodity derivatives?*

51. Respondents asked for CESR to undertake a comparison of the different accepted market practices across the EU. CESR believes that this is an area more suitable for discussion at level 3.

Lists of Persons having access to Inside Information

52. CESR received many comments and representations in this area. Consequently, CESR has substantially revised its advice as a result of the outcome of consultation, particularly with regard to respondents' desire for a less bureaucratic and more flexible method of adherence to the obligations in the Directive.

Key Issues

53. The trigger point for creating a list. Some respondents were concerned that CESR was extending the scope of the obligation in the Directive by calling for lists to be created prior to information being inside information. Other respondents wanted CESR to clarify when information becomes "inside". To avoid misunderstanding, CESR has added a new paragraph (31) to the explanatory text. This states that questions about what constitutes inside information and when information becomes inside should be answered with reference to the Directive and the level 2 measures relating to the definition of inside information.

54. The compliance costs of tracking information within an organisation would be disproportionate to the regulatory benefit. There was widespread concern that there would be a surfeit of information, of which some would be inappropriate or unnecessary and that this would render it far harder to actually establish who was an insider. Part of the problem was that the criteria were too broadly defined. Some feared that even a minor piece of information might trigger the need for a new list and thus compliance costs would disproportionately increase. CESR accepts the comment that a balance should be maintained between improving the quality of information and the associated compliance burden. It has re-examined the advice and has simplified and streamlined its approach so that the criteria for drawing up and updating lists are clear and flexible and should allow issuers to meet their obligations under the Directive without incurring undue costs or difficulty.

55. A majority of respondents objected to CESR's proposed split between ad hoc and permanent lists. It was felt that ad hoc lists should be explicitly connected to when the disclosure of information was delayed, in accordance with article 6(1) and only for a limited list of significant incidents. Many proposed an approach which would consist of just permanent lists or of permanent lists combined with transaction or project specific lists.

56. Some deemed permanent lists less useful than lists for specific cases of inside information. Many made the point, accepted by CESR, that the purpose of ad hoc lists would generally be to aid a future investigation and that an excess of information should not be held when only a few lists would be subject to examination in the course of an investigation. Some therefore felt that it should be acceptable to be able to draw up a list upon request and that a firm would be in compliance as long as it was able to provide accurate, contemporaneous information about which staff possessed inside information. CESR thinks that it would be of limited use to create a list ex post since an investigation might be started several years after an incident, for example.

57. Some respondents questioned whether the text of the directive did require both permanent and ad hoc lists. CESR's belief is that the directive imposes a clear requirement to draw up lists of people with access to inside information. However, these do not necessarily have to be permanent or ad hoc lists.

58. CESR has acknowledged respondents' comments and has adopted a different approach. CESR's advice now makes a distinction between habitual and occasional access. Our purpose is to capture the people who have access to inside information, either because of their function or because they were given such access on a particular basis. An issuer must create and update a

list (or lists) which will meet the requirements of the new paragraph 34. If an individual receives access to inside information then the list must be updated.

Other Comments

59. CESR has modified its advice so that the need for "dedicated resources" is no longer explicitly addressed. Instead, the explanatory text comments that it is necessary for issuers to have "adequate systems, controls and procedures" and this is in keeping with CESR's desire to increase flexibility in this area.

60. CESR has not requested that a list provide any detail about the inside information as it recognises that this would be too onerous a requirement. The reason why the person is on the list will provide sufficient indication of the person's involvement and the nature of the information to which they have access.

61. CESR also wishes to clarify that changes in information do **not** trigger the need to update lists. Changes in the personnel with access to inside information do.

62. Respondents commented that the information on a list should **have** to have a significant influence on the market. The inside information to which those on the list have access will, by definition, be likely to have an impact on the price of relevant financial instruments. In addition, CESR, in the explanatory text, states that the list should indicate, in general terms at least, the nature of the inside information to which the person listed has access.

63. The wording of paragraph 61 was insufficient since it would only cover employees of the issuer and thus not anyone else who might have access to inside information. CESR has changed this in the revised advice and persons who are working for the issuer, whether under a contract of employment or not, should be listed each time that they obtain access to inside information.

64. CESR accepted that there was a need to clarify what obligation firms had to keep lists. CESR's advice now states that a record of the list must be kept for at least five years.

Questions

Question 10: *Do you agree on the relevance of establishing a list for each matter or event when it becomes inside information?*

65. The most common response was no. Respondents sought a solution that would allow a choice between permanent and ad hoc lists. There is certainly a distinction between a permanent list intended to prevent market abuse and an ad hoc list to assist an investigation and some felt that this meant that only permanent insiders should appear on the permanent list. Some were in favour of a permanent list by function.

66. CESR has sought to achieve a flexible solution to the question of differentiating the type of list.

67. There was discussion of the definition of "matter" and "event" with the suggestion that "event" be limited to major occurrences outside the normal course of business or which would have a material impact on the company's revenues or profits. CESR's revised advice renders this distinction immaterial.

Question 11: *Should the minimum content of the list be specified at Level 2?*

68. The consensus was that it should but there were quite a few respondents who felt that it should not. Banks and issuers, in particular, wanted a precise definition of content at level 2.

69. Some felt an amendment was necessary to take account of the fact that it was not always possible to define at which point in time one gained or lost access to inside information. CESR has clarified in a new paragraph 33 when the list should be reviewed and updated.

Question 12: *Should Level 2 give examples of those persons acting on behalf of or for the account of the issuer who should be required to draw up lists?*

70. Many respondents sought guidance as to who was captured by the phrase: "acting on behalf". Some, however, felt that this was a level 3 issue. This is CESR's position and, accordingly, original paragraph 62 has been removed.

Question 13: *To what extent is drawing up a list of "permanent insiders" useful? Should Level 2 identify the jobs which typically provide access to inside information?*

71. Some felt that a list of jobs that gave access to inside information would be helpful but the consensus was that this should be agreed at level 3, if at all. It was also noted that such a list should be illustrative and not exhaustive or prescriptive.

72. Most issuers hoped to restrict their obligation to just a permanent list. CESR's revised advice is intended to provide additional flexibility for an issuer.

Question 14: *Would it be useful to further develop at Level 3 the "illustrative system" outlined?*

73. Respondents generally felt that this would be beneficial. Some disagreed however.

Question 15: *Would it be useful to describe the meaning of the expression 'working for them' (article 6, paragraph 3) for example, to give clarification regarding people who are not employees of the issuer?*

74. Many respondents felt that this would be useful although a few believed that it was not necessary. Some also sought further explanation for working on a long-term basis. Others felt that only those who had a contractual relationship to the issuer that gave them access to the relevant inside information should be included. After further consideration, CESR has re-examined its position and maintains its view that the level 1 text is self-executing and does not require further explanation.

Question 16: *Do you agree with the approach adopted regarding the criteria which trigger the duty to update insiders' lists?*

75. Some agreed with the approach for permanent lists but disagreed for ad hoc lists while others believed the approach was incorrect in both instances. CESR agrees with this remark and has sought, therefore, a more flexible solution.

76. Some felt that it was impossible to hold the issuer responsible for the update of lists or the dissemination of information held by outside bodies. CESR does not accept the first comment and the second is not something that CESR has suggested.

Disclosure of Transactions

77. Comments in this area concentrated on the scope of application.

Key Issues

78. The question of thresholds was the subject of much discussion. Some respondents were enthusiastic about thresholds and felt that the disclosure of minuscule transactions would reduce transparency and potentially mislead the market by swamping the market with disclosures. In general, respondents tended to favour a threshold figure that accorded with the current law in their jurisdiction. Many were opposed to the concept of thresholds per se, with concerns expressed about the cost of monitoring a series of small transactions. CESR was not unanimous in this area but has decided that it will not recommend the utilisation of thresholds. Many jurisdictions do not have thresholds and the market has not suffered from too much disclosure in this area. Furthermore, many members of CESR are of the view that those people within the scope of the directive should be dissuaded from trading their shares for small transactions.

79. The proposal captured too many people for whom disclosure would not be useful or proportionate. Some felt that the scope should be limited to the people who constituted the administrative, management or supervisory bodies or who were linked to the issuer as a partner since the greater the number of people reporting, the greater the risk of the market being overwhelmed with information. In certain jurisdictions, the management and supervisory bodies contain all decision-making functions so there is no need for an extension of the definition. It also seemed problematic to extend the obligation to people inhabiting the same house. It was felt after consultation that this did not have the intended results and it would be better to restrict applicability to spouses (or their equivalents in national laws), dependent children and relatives who inhabited the same house on a long-term basis.

80. The European Commission is of the view that inheritances, the acceptance of a gift, and compensation and remuneration arrangements, do not constitute a transaction within the meaning of Art. 6 (4) of the Directive. CESR has accepted this view in its advice. However, a majority of CESR members believe that, with the exception of inheritances, the duty to disclose should also apply to these activities. Actions in these areas by those people within the scope of the directive are relevant to preserving market integrity and should be disclosed.

Other Comments

81. There was no consensus over the time for disclosure. Several respondents suggested five working days but some thought three, or even two, were too many. After further consideration, CESR has decided that the disclosure should be made to the competent authority "within three working days from the trading date". This limit is intended to provide flexibility and is not intended to prevent earlier disclosure, where this is possible.

82. Several respondents asked that a link be established so that a list held of permanent insiders should be the list of individuals who are subject to the disclosure requirements. CESR believes that such a link would be inappropriate since there may be individuals who do not have habitual access to inside information but who should be subject to the disclosure requirements.

Questions

Question 17: *Is the above description for "persons discharging managerial responsibilities within an issuer" sufficient for level 2 legislation? Are there other persons that should be considered as*

belonging to the management of the issuer or should there be a specific restriction to persons who can assess the economic and financial situation of the company?

83. The majority opinion was that the description was insufficient. Some did think that the specific detail should be left to level 3. If too many people had to disclose their transactions then the transparency and utility of the information would be lessened.

84. Some respondents wanted to restrict the disclosure obligations solely to members of the board. CESR rejects this change, as it would exclude significant individuals who should be captured. In some jurisdictions the management and supervisory bodies contain all decision-making functions so there is no need for an extension of the definition.

85. CESR has revised its explanatory text to clarify the individuals who should be subject to the disclosure requirements. The feedback suggested that inappropriate levels of management; for example those with responsibility for a limited part of the company but without the ability to influence the company as a whole, were being captured. A new paragraph (42) now explains that persons discharging managerial responsibilities within an issuer means in principle the members of the administrative, management or supervisory bodies (i.e. those with high level authority and responsibility). In some countries there are also "top executives", who are outside these bodies but have decision making power to decide on the future development and business prospects of the issuer. The disclosure requirement also applies to them.

86. CESR has been mindful of the need to balance the utility of the information requested with the regulatory burden imposed. It has therefore modified the information required in a notification to exclude the requirement for an address.

87. It was requested that CESR should clarify what actions and due diligence competent authorities would undertake with the disclosed transactions they received. CESR believes that this is outside the scope of the mandate.

Question 18: *Is the above description sufficient for level 2 legislation? Are there other persons that should be considered as belonging to this category?*

88. Many felt it was sufficient but there were also strongly expressed opinions that the expression was too broadly defined. Some felt that the expression "persons sharing the same household" would constitute a breach of article 8 of the ECHR and was an inappropriate obligation. CESR accepts that someone living in the same house is not a sufficient connection to require that person to disclose his or her transactions.

89. CESR has revised its proposal in accordance with the broad tenor of the consultation responses, though there were differences in the degree of change requested. CESR's final advice states that the requirement should fall upon family and partners living on a long-term basis in the same house as the individual who exercises managerial responsibilities' house. Dependent children and spouses would be covered whether or not they lived in the same house.

Question 19: *Is the above description sufficient for level 2 legislation? Should there be a threshold concerning the disclosure obligation to the competent authority?*

90. Respondents were strongly divided upon the issue of thresholds. Some were enthusiastic and felt that the disclosure of minimal transactions would reduce transparency and the usefulness of the information. Others opposed thresholds, describing them as arbitrary and inviting circumvention. Some respondents did not support their existing national threshold arrangements. The difference in the size and liquidity of the various European markets means

that a transaction which might be viewed as minor in one market, might well be of significance in another market and that this means a useful pan-European threshold figure would be impossible to establish.

91. Consequently, "CESR, almost unanimously, proposes not to include thresholds as the disclosure obligations could be easily circumvented. Furthermore, it is not possible to find a common threshold due to the diversity of EU markets in terms of structure and liquidity. One member maintains the view that a threshold for disclosing transactions should be proposed.

Question 20: *Is the above description sufficient for level 2 legislation? Are there any other details that should be covered on this level, for example the number of the relevant securities that the person holds after the transaction?*

92. Respondents generally felt that the description, as it stood, was sufficient

93. Many industry respondents felt that disclosing the number of relevant securities held after the transaction was unnecessary and an infringement of privacy. CESR accepts such a requirement would be outside the scope of Art. 6 (4).

Suspicious Transactions

94. The tenor of the consultation feedback was that there needed to be an appropriate balance between the need to notify suspicious transactions and the danger that too many transactions would be reported to the competent authority, which would render such notifications useless. CESR was determined to achieve this balance and has modified its advice accordingly.

Key Issues

95. Numerous respondents expressed the belief that notifying the regulatory authority in good faith should constitute a safe harbour from legal liability. CESR has commented in its explanatory text that this is not something that may be addressed at level 2. The duty to report a suspicious transaction should provide a legal defence for a firm acting in good faith.

96. The responsibility for investigating whether or not a transaction is suspicious should not be placed on the reporting party. CESR's advice was felt to be unclear and ambiguous since a reporting party needed no evidence but did need "sufficient indications". CESR's advice has been revised, in a new paragraph 55, to address these points. This states that there is a balance between the requirements stated in Article 6.9 of the Directive and the fact that it is the responsibility of the competent authority to investigate whether or not a transaction constitutes market abuse. The trigger for reporting is not evidence but "sufficient indications". An obligation to notify the competent authority will only arise if facts have emerged which lead to the conclusion that the transaction might be regarded as insider dealing or market manipulation within the Market Abuse Directive. It is stressed in the explanatory text that CESR considers that the Directive does not require the notifying person to be in possession of evidence. However, internal procedures should be established to assess and explain what would constitute a "sufficient indication".

Other Comments

97. Several of the comments received focused on the need to define a suspicious transaction. Besides the level 1 provisions, CESR in its first set of Level 2 Implementing Measures for the Market Abuse Directive regarding the definition of market manipulation, provided non-exhaustive factors and diagnostic flags. Reference to these is made in this second set of advice. While these are intended for the use of the competent authority, they may also be employed by others to give a better understanding of what may constitute a suspicious transaction and thus a sufficient indication to necessitate a report.

98. CESR has inserted an additional paragraph (61) in the explanatory text which states that competent authorities should consult "to ensure a degree of certainty about the elements that trigger the duty to disclose suspicious transactions, in order to facilitate the decisions made by intermediaries. This should underpin a common and workable approach within the internal market." This could, in time, be the source of further guidance in this area.

99. Respondents felt that the timeframe for reporting should be longer to allow for internal due process. Therefore "immediately" should read "as soon as possible" or "promptly" to give greater leeway. CESR has amended (original) paragraph 96 to reinforce that notification without delay means immediately after the person becomes aware of any fact as a result of which the transaction seems to be suspicious. Some commented that the proposed advice requested a long list of particulars for a notification and thus asked for more time to be available so that they could gather the required information. In response to this, CESR has

introduced a more flexible approach, whereby, "the person subject to the notification obligation shall include in his notification as much information … as possible".

100. Respondents stressed that the responsibility for notification should not be placed on the employees of the person professionally arranging transactions. CESR's explanatory text clarifies this: "Although the employees…are not subject to any notification duty themselves, their collaboration is of course an important element. In this perspective, the existence of internal procedures which make the employees aware of the notification duty is advisable".

Questions

Question 21: *Do you agree with the proposed approach?*

101. Many did not agree as they felt it should not be incumbent on the reporting party to provide evidence for their suspicion or to investigate a suspicious transaction. Investment services firms and banks strongly criticised the approach. They wanted greater legal security to deal with the conflict between the confidentiality of customer information and the obligation to report. CESR agrees that it is sufficient for a party to have reason to suspect but no evidence or proof of its allegation (though there must be some basis for suspicion). It has revised its advice accordingly therefore. CESR does not believe that the responsibility to report suspicious transactions should conflict with a firm's separate responsibility to notify the relevant authorities where money laundering is suspected.

Question 22: *Do you think that other possibilities should be taken into account?*

102. Some respondents wanted notification of a doubtful transaction to be immediate and that this should be regardless of whether or not the transaction had actually taken place. CESR recognises the value of this but it notes that it is outside the scope of the level 1 text.

Question 23: *Do you think that other elements should be mentioned?*

103. The consensus was that there was no need for other elements to be mentioned.

104. Some respondents suggested that a convergence of reporting practices should be a part of level 3 discussions.

105. Respondents requested a definition of transaction at level 2. CESR does not provide definitions of terms at level 2 unless asked to do so. Paragraph 69 (new) explains that transactions is as referred to in Article 6.9 of the Directive and includes "any transaction entailing a transfer of financial instruments.

106. CESR has rejected the request that the notion of a group of transactions be deleted as this might mean that transactions that should be reported as suspicious, because of their linkage within a group, were missed.

Question 24: *Do you think that the proposed advice is appropriate?*

107. Respondents felt that the advice was broadly appropriate but pointed out the problems already mentioned. The most substantial worry was over the notification of a transaction that subsequently turned out to be acceptable. CESR does not believe that its advice will expose market participants, acting in good faith, to additional legal risk in this regard.

108. The concerns expressed by respondents were generally connected to the duty to report suspicious transactions itself. This is a level 1 issue and therefore not something that CESR should address at level 2.

Annex 1
Consultation Responses
Banking

European Association of Co-operative Banks
Austrian Banking Association
Realkreditradet
Danish Bankers Assoc and Danish Securities Dealers Assoc
BN Paribas
FBE
Zentraler Kreditausschuss
BVR
Association of German Banks
Deutscher Sparkassen und Giroverband ev.
Mediobanca
NVB
BBA

Financial Analysts/Credit Rating Agencies

Moodys
Standard and Poors

Government/Regulatory/Enforcement

Insurance/Pension/Asset Managers

Investors

Investment Services

AFEI
Assiosim
RWE Trading GmbH
Institut der Wirtschaftsprufer
Association of Greek Institutional Investors
Unionsim
Association of Norwegian Stockbroking Companies
IPMA
International Securities Market Association
FOA
Institute of Chartered Accountants in England and Wales
International Swaps and Derivatives Association
European Federation of Energy Traders

Issuers

Assonime
Federationdes Entreprises de Belgique
Danish Shipowners Association
Confederation of Finnish Industry and Employers
AFEP
European Association for Listed Companies

Medef
Deutscher Investor Relations Kreis (DIRK)
Software AG
Hawesko Holding AG
SAP Systems Integration
Deutsche Telekom
Deutsches Aktieninstitut e V
AWD Holding AG
Infor
De Brauw Blackstone Westbroek
VEUO
Quoted Companies Alliance
CBI

Legal Profession

Uria and Menendez
SJ Berwin
Law Society of England and Wales

Regulated Markets/Exchanges

Federation of European Securities Exchanges
Copenhagen Stock Exchange
HEX Group
EEX, Nord Pool and Powernext
Warenterminboerse Hannover AG
Hellenic Exchanges SA et al
Borsa Italiana
Bolsa de Madrid
London Metal Exchange
International Petroleum Exchange
London Stock Exchange