



## **Market Abuse Directive**

**Level 3 – Third set of CESR guidance and  
information on the common operation of the  
Directive to the market**

### **Public Consultation**

May 2008



## Index

### Introduction

### Draft Third set of CESR Guidance on the Operation of the Market Abuse Directive

#### I INSIDERS' LISTS

#### II SUSPICIOUS TRANSACTION REPORTS



## Introduction

1. CESR is continuing in its efforts to prepare ground for convergent implementation and application of the Market Abuse regime by ensuring that a common approach to the operation of the Directive takes place throughout the EU amongst supervisors. In July 2007, CESR confirmed that CESR-Pol will undertake another stream of Level 3 work on market abuse on the basis of the mandate given by CESR to CESR-Pol concerning Level 3 of the Market Abuse Directive (MAD) (Ref. CESR/04-10c) which should be read in conjunction with the Terms of Reference of CESR-Pol (Ref. CESR/06-114 replacing CESR/02-070b) and in the light of the responses to the Call for Evidence (Ref. CESR/06-664). In its Work Program (CESR/07-416), CESR has informed the market about the issues to be covered in a 3<sup>rd</sup> set of guidance:
  - Harmonisation of requirements for insiders lists
  - Suspicious Transactions Reporting (STRs)
  - Stabilisation Regime as Level 3
  - The notion of inside information to be analysed as a Level 3 topic.
2. This set of guidance will be published for European-wide consultation in two steps: A first consultation paper will cover the topics on insider lists and STRs and will be published for consultation over summer and a second consultation paper dealing with the topics on stabilization and the notion of inside information shall be published later this year.
3. For the first two topics, a survey has been undertaken based on questionnaires sent out to all CESR members. The work already conducted by CESR on Level 2 implementing measures for the MAD has been also taken into consideration, where appropriate. On the basis of the responses received during the surveys, CESR-Pol has developed the following guidance for the market and CESR members.
4. Two more subjects that have been identified in the work programme for further guidance, i.e. the mapping of the existing thresholds in Member States and other practices regarding directors' dealings as well as possible guidance on the definition of inside information with regard to commodity derivatives to the extent possible, have not been considered as having the same priority level and will be addressed at a later point of time.
5. Interested parties are welcome to submit their comments to the draft guidance set out in this paper and send their responses via CESR's website ([www.cesr.eu](http://www.cesr.eu)) under section "Consultations". The consultation closes on 30 September 2008.

## Draft Third set of guidance on the operation of the Market Abuse Directive

### I. INSIDERS LISTS

#### Purpose:

6. Discussion of potential market questions regarding the harmonization of requirements for insiders lists as provided in Directive 2003/6/EC of the European Parliament and the Council on Insider Dealing and Market Manipulation (Market Abuse) (hereinafter referred to as “the Directive”).

#### Relevant articles of the Directive

7. Article 6 (3) of the Directive 2003/6/EC states that “Member States shall require that issuers, or persons acting on their behalf or for their account, draw up a list of those persons working for them, under a contract of employment or otherwise, who have access to inside information. Issuers and persons acting on their behalf or for their account shall regularly update this list and transmit it to the competent authority whenever the latter requests it.”
8. Article 5 of the Directive 2004/72/EC implementing Directive 2003/6/EC as regards accepted market practices, the definition of inside information in relation to derivatives on commodities, the drawing up of lists of insiders, the notification of managers' transactions and the notification of suspicious transactions states that:

- (1) *“For the purposes of applying the third subparagraph of Article 6(3) of Directive 2003/6/EC, Member States shall ensure that lists of insiders include all persons covered by that Article who have access to inside information relating, directly or indirectly, to the issuer, whether on a regular or occasional basis.*
- (2) *Lists of insiders shall state at least: (a) the identity of any person having access to inside information; (b) the reason why any such person is on the list; (c) the date at which the list of insiders was created and updated.*
- (3) *Lists of insiders shall be promptly updated (a) whenever there is a change in the reason why any person is already on the list; (b) whenever any new person has to be added to the list; (c) by mentioning whether and when any person already on the list has no longer access to inside information.*
- (4) *Member States shall ensure that lists of insiders will be kept for at least five years after being drawn up or updated.*
- (5) *Member States shall ensure that the persons required to draw up lists of insiders take the necessary measures to ensure that any person on such a list that has access to inside information acknowledges the legal and regulatory duties entailed and is aware of the sanctions attaching to the misuse or improper circulation of such information.”*

#### CESR Guidance

9. In July 2007, CESR published a Level 3 document – the 2<sup>nd</sup> Set of Guidance and information on the common operation of MAD (Ref: CESR/06-562b) - wherein section IV deals with the issue of insiders’ lists.

#### Guidance to the market

10. After four years of operation of the Market Abuse Directives, insiders' lists are expected to have raised the importance that companies put on the careful handling of inside information and helped issuers to monitor the flow of inside information and hence to comply with their duties of secrecy. CESR members are generally satisfied with the quality of information received so far through insiders' lists, taking into consideration that insiders' lists should fulfill the requirements of completeness and preciseness, as set out in the relevant legislation. There is a common understanding amongst CESR members that insiders' lists are used by the competent authorities as a first instance tool in a market abuse enquiry or investigation, without prejudice for the authority to require additional information from the issuer, as it is usually done, when a case is investigated.
11. As stated in CESR's 2<sup>nd</sup> set of Guidance on the operation of the MAD (Ref. CESR/06-562b): *"it should be recalled that the requirements to keep, maintain and provide the competent authority with insider lists only applies to the issuer that has requested or approved admission of its financial instruments to trading on a regulated market in a Member State (Article 9(3) MAD)"*. The following three possible ways of practical application of the obligation to prepare insiders' lists have been identified without having ascertained any conflicting consequences in practice depending on the option followed: either in cases where third persons acting on behalf or for the account of the issuers are required to send their own insiders' lists to the competent authorities, or in cases where it is left to the discretion of the issuer and the third persons acting on its behalf to send to the competent authority the insiders' lists, or in cases where it is the issuers who are required to send the lists for third persons acting on their behalf or for their account. CESR considers that the issuer should make these third persons aware that all persons who might be expected to have access to inside information are to be included in the insiders' lists, which are sent to the competent authorities.
12. Having access to inside information is a matter of fact, which triggers the obligation to include a person in an insiders' list. Whilst CESR understands that companies may feel that many people within the organization need to know some inside information, there are clearly risks associated with large numbers of people having access to such information and issuers should make every effort to keep inside information known to as small a group of people as possible. CESR's experience to date shows that insiders' lists often have very large numbers of names on the list. To be included by a company on its insider list, the concept of having access to inside information means that the person concerned must have access to information as a result of his activities or duties within the issuer or persons acting on their behalf, as opposed to obtaining access by other means, such as by accident, of which the issuer is not aware.
13. CESR is of the view that the emphasis should rather be given to the access (regular/occasional) of persons to inside information related directly or indirectly to issuers than to the existence of a legal distinction between regular and occasional insiders.
14. Possessing inside information triggers the prohibition from disclosing and using inside information for insider dealing as provided in articles 2 and 3 of MAD, irrespectively of the way the information has been obtained.
15. Insiders' lists can contain, among others, specific categories of persons within an issuer, who have regular access to inside information. Typically, these people might include: members of the board of directors, CEOs, relevant persons discharging management responsibility, related staff members (such as secretaries and personal assistants), internal auditors, people having access to databases on budgetary control or balance sheet analyses, people who work in units that have regular access to inside information (such as IT people).
16. Professionals acting on behalf of the issuers are also included in the insiders' lists. Examples of such professionals would include, but not be limited to, auditors, attorneys, accountants and tax advisors, managers of issues (like corporate and investment banks), communication and IT agencies, rating agencies, and investor relations agencies. In all jurisdictions of CESR members the legislation does not limit the scope of the professionals providing services to



the issuers to be included in the insiders' lists. The general rules on drawing up insiders' lists are applicable.

17. Issuers may want to outsource the preparation of insiders' lists. In this context CESR points out that the decision of outsourcing to third parties of the drawing up the lists of insiders by issuers rests with the issuer. Most CESR members do thus not see any serious difficulties related to the outsourcing of drawing up the lists of insiders, subject to certain conditions, such as the requirement that the issuer retains fully its responsibility, as derived by Article 9 (3) MAD and that the delegated persons are also included in the lists.
18. As stated in CESR's 2<sup>nd</sup> set of Guidance on the operation of MAD: *“it should be noted that under the MAD a competent authority only needs to be supplied with an insiders' list if it requests it from the issuer: there is no obligation on an issuer spontaneously to provide its insider list to the competent authority or inform it of updates to the list”*. Insiders' lists are sent to the competent authorities either by letter, fax and/or e-mail, all of which methods are considered sufficient by CESR. Insiders' lists are prepared in their domestic official language but CESR members would be willing to accept insiders' lists submitted to them in a foreign language other than their official language, should this language be customary in the sphere of international finance.
19. CESR considers that insiders' lists might be submitted in a foreign language:
  - either by a multi listed issuer or
  - by a third person acting on behalf or for the account of an issuer, if required to send its own insiders' list to the competent authority, where relevant in national law, if not using the same language as that of the issuer,

provided that this language is customary in the sphere of international finance. (see also CESR's 2<sup>nd</sup> set of Guidance: *“For issuers subject to the jurisdiction of more than one EU or EEA Member State with respect to insider list requirements, it is recommended that the relevant competent authorities recognise insider lists prepared according to the requirements of the Member State where the issuer in question has its registered office.”*).

**Question to the market: Market participants are requested to indicate if there are any further issues for consideration by CESR, providing also the reasons why.**



## II. SUSPICIOUS TRANSACTIONS REPORTS

### Purpose:

20. Discussion of potential market questions regarding Suspicious Transaction Reporting as provided in Directive 2003/6/EC of the European Parliament and the Council on Insider Dealing and Market Manipulation (Market Abuse) (hereafter referred to as “the Directive”).

### Relevant articles of the Directives

21. Article 6 (9) of the Directive 2003/6/EC states that “*Member States shall require that any person professionally arranging transactions in financial instruments who reasonably suspects that a transaction might constitute insider dealing or market manipulation shall notify the competent authority without delay.*”
22. Articles 7 to 11 of the Directive 2004/72/EC implementing Directive 2003/6/EC as regards accepted market practices, the definition of inside information in relation to derivatives on commodities, the drawing up of lists of insiders, the notification of managers' transactions and the notification of suspicious transactions state that:

#### ***Article 7 - Suspicious transactions to be notified***

*For the purposes of applying Article 6(9) of Directive 2003/6/EC, Member States shall ensure that persons referred to in Article 1 point 3 above shall decide on a case-by-case basis whether there are reasonable grounds for suspecting that a transaction involves insider dealing or market manipulation, taking into account the elements constituting insider dealing or market manipulation, referred to in Articles 1 to 5 of Directive 2003/6/EC, in Commission Directive 2003/124/EC (1) implementing Directive 2003/6/EC as regards the definition and public disclosure of inside information and the definition of market manipulation, and in Article 4 of this Directive. Without prejudice to Article 10 of Directive 2003/6/EC, persons professionally arranging transactions shall be subject to the rules of notification of the Member State in which they are registered or have their head office, or in the case of a branch, the Member State where the branch is situated. The notification shall be addressed to the competent authority of this Member State. Member States shall ensure that competent authorities receiving the notification of suspicious transactions transmit such information immediately to the competent authorities of the regulated markets concerned.*

#### ***Article 8 - Timeframe for notification***

*Member States shall ensure that in the event that persons, as referred to in Article 1 point 3, become aware of a fact or information that gives reasonable ground for suspicion concerning the relevant transaction, make a notification without delay.*

#### ***Article 9 - Content of notification***

*1. Member States shall ensure that persons subject to the notification obligation transmit to the competent authority the following information:*

- (a) description of the transactions, including the type of order (such as limit order, market order or other characteristics of the order) and the type of trading market (such as block trade);*
- (b) reasons for suspicion that the transactions might constitute market abuse;*
- (c) means for identification of the persons on behalf of whom the transactions have been carried out, and of other persons involved in the relevant transactions;*
- (d) capacity in which the person subject to the notification obligation operates (such as for own account or on behalf of third parties);*
- (e) any information which may have significance in reviewing the suspicious transactions.*

*2. Where that information is not available at the time of notification, the notification shall include at least the reasons why the notifying persons suspect that the transactions might constitute insider dealing or market manipulation. All remaining information shall be provided to the competent authority as soon as it becomes available.*



**Article 10 - Means of notification**

*Member States shall ensure that notification to the competent authority can be done by mail, electronic mail, telecopy or telephone, provided that in the latter case confirmation is notified by any written form upon request by the competent authority.*

**Article 11 - Liability and professional secrecy**

*1. Member States shall ensure that the person notifying to the competent authority as referred to in Articles 7 to 10 shall not inform any other person, in particular the persons on behalf of whom the transactions have been carried out or parties related to those persons, of this notification, except by virtue of provisions laid down by law. The fulfilment of this requirement shall not involve the notifying person in liability of any kind, providing the notifying person acts in good faith.*

*2. Member States shall ensure that competent authorities do not disclose to any person the identity of the person having notified these transactions, if disclosure would, or would be likely to harm the person having notified the transactions. This provision is without prejudice to the requirements of the enforcement and the sanctioning regimes under Directive 2003/6/EC and to the rules on transfer of personal data laid down in Directive 95/46/EC.*

*3. The notification in good faith to the competent authority as referred to in Articles 7 to 10 shall not constitute a breach of any restriction on disclosure of information imposed by contract or by any legislative, regulatory or administrative provision, and shall not involve the person notifying in liability of any kind related to such notification.*

**CESR Guidance**

23. In May 2005, CESR published a Level 3 document – the 1<sup>st</sup> Set of Guidance and information on the common operation of MAD (Ref: CESR/04-505) - wherein section V deals with the issue of Suspicious Transaction Reports (STRs). In this first guidance CESR developed a format to be used for STRs to be sent to the competent authorities under the Directive.

**Guidance to the Market**

24. CESR members emphasize that, based on the four years of experience after the implementation of the MAD, STRs are very useful and helpful in market abuse investigations.
25. CESR reminds that, without prejudice to the obligations stipulated by the MiFID, any person professionally arranging transactions in financial instruments who reasonably suspects that a transaction might constitute insider dealing or market manipulation shall notify the competent authority.
26. The member of CESR are aware that there are uncertainties in the market as to the decision when to inform the competent authority of suspicious transactions as well as to uncertainties about the content of the STRs. Above that it was raised in the Call for Evidence on the market abuse regime that it was also not commonly clear which CESR member would be competent authority to receive such notifications.

**A. Criteria for determining the notifiable transactions shall include the following:**

27. CESR is of the view that where an unexecuted order for a transaction gives rise to a suspicion of market abuse, this suspicion is strongly recommended, when not already legally required on a national basis, to be reported to the competent authority. For example, when an institution refuses to place an order in the order book, the placing of the order with the institution, if suspicious, is strongly recommended to be notified to the competent authority.



28. The entities subject to the notification requirement should be aware that not only equity regulated market related suspicious transactions need to be reported but also those suspicious transactions which involve instruments that are admitted to trading in non-equity regulated markets (inter alia debt, derivatives and commodity derivatives markets).
29. CESR would like to remind intermediaries who are under the obligation to do such notifications, that a STR can be reported by telephone so long as, in such case, this is followed up by a confirmation in any written form upon request by the competent authority.

B. The following information may be included in the notification to the competent authority:

30. Article 9(1)e of implementing Directive 2004/72/EC states that '*Any information and documents which may have significance in reviewing the case*' should be included in the STR.
31. Acknowledging that the information to be delivered is to be assessed on a case-by-case basis and depends on the surrounding context, CESR members consider it helpful to provide examples of the types of information that may be included or attached to an STR. It must however be noted that the following is a non-exhaustive and purely indicative list of examples. This means that when the information is readily accessible for the firm and can be easily attached (electronically or otherwise) to the notification, the members of CESR would expect the firms to endeavour to include such information. The emphasis for the firms should lie with the timeliness and accuracy of the notification. CESR recommends that notifying institutions include the following information in an STR:
  - The name of the person(s) at the notifying institution who had direct contact with the client who placed the suspicious order;
  - Relevant news items or articles, which contributed to the forming of a reasonable suspicion of market abuse;
  - When the suspicion is based upon a trade or series of trades which are out of line with the usual trading of the client, a complete explanation of why the transaction or order is unusual for this particular client and if easily obtainable, relevant account documents which would support this conclusion such as, for example, a copy of the client's investment profile;
  - Information concerning the employment of the client about whom a suspicious order or transaction is reported – this information can often be gleaned from account opening documents, e-mail addresses of the client, a copy of the clients business card or from other account related information;
  - Tapes of relevant conversations between the firm and her client – such tapes should not only be limited to the conversations in which the order was given but also to all other potentially relevant conversations that could prove the suspicious aspect of the transaction, such as, for instance, the moment of the sale of securities following a price-sensitive news event.
32. The institution has to make an appropriate assessment of all the elements. CESR would like to emphasize that the responsibility for determining whether to report suspicious transactions and to what extent to provide accompanying information rests solely with the intermediary.
33. CESR members are open to discuss with institutions whether a particular order or transaction should be reported.
34. CESR members encourage institutions to keep records of cases of potentially suspicious transactions that have been examined but which have not been reported to the competent authorities.
35. CESR reminds institutions that a broker or any concerned individual within the institution, who has suspicion about an order or a transaction consults about the need to notify it internally or within the group, (with for instance the relevant compliance officer(s)),



provided that confidentiality is safeguarded. Thus such consultation should be limited to the persons who have to be informed according to the legal obligations or the internal rules of the institution. In addition, CESR wishes to emphasize that, in no circumstance, the persons concerned by the suspicion or the STR or any related persons be ‘tipped off’.

36. Additionally, CESR considers the training of personnel in the recognition and reporting of suspicious transactions absolutely vital, as it plays an important role in increasing the number and quality of STRs.
37. CESR members have tried to accommodate the concern of market participants to be required to establish complex and costly structures and recognize that there is no explicit legal requirement to have specific technical reporting mechanisms in place to detect and identify suspicious transactions. As this issue was raised in the Call for Evidence, CESR members expect that appropriate systems have been adopted by the institutions. The extent to which these systems include IT tools is a question for the entity concerned.

**Question to the market: Market participants are requested to indicate if there are any further issues for consideration by CESR, providing also the reasons why.**

\*\*\*\*\*