

**Proposal for a Directive of the European Parliament and of the Council on insider dealing and market manipulation (market abuse)**

(2001/C 240 E/32)

COM(2001) 281 final — 2001/0118(COD)

*(Submitted by the Commission on 1 June 2001)*

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 95 thereof,

Having regard to the proposal from the Commission,

Having regard to the opinion of the Economic and Social Committee,

Having regard to the opinion of the Committee of the Regions,

Acting in accordance with the procedure laid down in Article 251,

Whereas:

- (1) A genuine Single Market for financial services is crucial for economic growth and job creation in the Community.
- (2) An integrated and efficient financial market requires market integrity. The smooth functioning of securities markets and public confidence in markets are prerequisites for economic growth and wealth. Market abuse harms the integrity of financial markets and public confidence in securities and derivatives.
- (3) The Communication of 11 May 1999 from the Commission 'Implementing the framework for financial markets: action plan' <sup>(1)</sup> identifies a series of actions that are needed in order to complete the single market for financial services. Heads of State and Government, at the Lisbon Summit of April 2000, called for the implementation of that action plan by 2005. The action plan stresses the need to draw-up a Directive against market manipulation.
- (4) At its meeting on 17 July 2000, the Council set up the Committee of Wise Men on the Regulation of European Securities Markets. In its final report the Committee of

Wise Men proposed the introduction of new legislative techniques based on a four level approach, namely framework principles, implementing measures, cooperation and enforcement. Level 1, the Directive, should confine itself to broad general 'framework' principles while Level 2 should contain technical implementing measures to be adopted by the Commission with the assistance of a committee.

- (5) The Stockholm European Council Resolution endorsed the final report of the Committee of Wise Men and the proposed four level approach to make the regulatory process for Community securities legislation more efficient and transparent.
- (6) According to the Stockholm European Council Level 2 implementing measures should be used more frequently, to ensure that technical provisions can be kept up to date with market and supervisory developments and deadlines should be set for all stages of Level 2 work.
- (7) New financial and technical developments enhance the incentives, means and opportunities for market abuse: through new products, new technologies, increasing cross-border activities and the Internet.
- (8) The existing Community legal framework to protect market integrity is incomplete. Legal requirements vary between the jurisdictions of Member States, leaving economic actors often uncertain over concepts, definitions and enforcement. In some Member States there is no legislation addressing the issues of price manipulation and the dissemination of misleading information.
- (9) Market abuse consists of insider dealing and market manipulation. The objective of legislation against insider dealing is the same as legislation against market manipulation: to ensure the integrity of Community financial markets and to enhance investor confidence in those markets. It is therefore advisable to adopt combined rules to combat both insider dealing and market manipulation. A single Directive ensures throughout the Community the same framework for allocation of responsibilities, enforcement and co-operation.

<sup>(1)</sup> COM(1999) 232 final.

- (10) Council Directive 89/592/EEC of 13 November 1989 coordinating regulations on insider dealing <sup>(1)</sup> was adopted more than a decade ago. Given the changes in financial markets and in Community legislation since its adoption, that Directive should now be replaced, to ensure consistency with legislation against market manipulation. A new Directive is also needed to avoid loopholes in Community legislation which could be used for wrongful conduct and which would undermine public confidence and therefore prejudice the smooth functioning of the markets.
- (11) Insider dealing and market manipulation prevent full and proper market transparency, which is a prerequisite for trading for all economic actors in integrated financial markets.
- (12) Prompt and fair disclosure of information to the public enhances market integrity, whereas selective disclosure by issuers can lead to a loss of investor confidence in the integrity of financial markets. Professional economic actors must contribute to market integrity.
- (13) Member States and the European System of Central Banks or national central banks should not be restricted in carrying out monetary, exchange-rate or public debt management policy.
- (14) Stabilisation or trading in own shares can be legitimate, in certain circumstances, for economic reasons and should not, therefore, in themselves be regarded as market abuse. Common standards should be developed to provide practical guidance.
- (15) The widening scope of financial markets, the rapid change and the range of new products and developments require a wide application of this Directive to financial instruments and techniques involved, in order to guarantee the integrity of Community financial markets.
- (16) Establishing a level playing field in Community financial markets requires wide geographical application of the provisions governed by this Directive.
- (17) A variety of competent authorities in Member States, having different responsibilities, creates unnecessary cost and confusion among economic actors. A single competent authority, of an administrative nature guaranteeing its autonomy from economic actors and avoiding conflicts of interest, should be designated in each Member State to deal with market abuse.
- (18) A common minimum set of strong tools and powers for the competent authorities will guarantee supervisory effectiveness.
- (19) In order to ensure that a Community framework against market abuse is sufficient, any infringement of the prohibitions or requirements laid down by this Directive will have to be promptly and effectively sanctioned.
- (20) Increasing cross-border activities require improved co-operation and a comprehensive set of provisions for the exchange of information between national competent authorities.
- (21) In accordance with the principle of proportionality as set out in Article 5 of the Treaty, the objectives of the proposed measures, namely to prevent market abuse in the form of insider dealing and market manipulation, cannot be sufficiently achieved by the Member States and can therefore, by reason of the scale and effects of the measures, be better achieved by the Community. This Directive confines itself to the minimum required in order to achieve those objectives and does not go beyond what is necessary for that purpose.
- (22) Technical guidance and modifications to the rules laid down in this Directive may from time to time be necessary to take account of new developments on financial markets; the Commission should accordingly be empowered to make such modifications as are necessary after consulting the European Securities Committee established by Commission Decision 2001/. . /EC.
- (23) Since the measures necessary for the implementation of this Directive are measures of general scope within the meaning of Article 2 of Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission <sup>(2)</sup>, they should be adopted by use of the regulatory procedure provided for in Article 5 of that Decision.
- (24) This Directive respects the fundamental rights and observes the principles recognised in particular by the Charter of Fundamental Rights of the European Union,

HAVE ADOPTED THIS DIRECTIVE:

#### Article 1

For the purposes of this Directive:

1. 'Inside information' shall mean information which has not been made public of a precise nature relating to one or more issuers of financial instruments or to one or more financial instruments, which, if it were made public, would be likely to have a significant effect on the price of those financial instruments or on the price of related derivative financial instruments.

<sup>(1)</sup> OJ L 334, 18.11.1989, p. 30.

<sup>(2)</sup> OJ L 184, 17.7.1999, p. 23.

2. 'Market manipulation' shall mean:

- (a) Transactions or orders to trade, which give, or are likely to give, false or misleading signals as to the supply, demand or price of financial instruments, or which secure, by one or more persons acting in collaboration, the price of one or several financial instruments at an abnormal or artificial level, or which employ fictitious devices or any other form of deception or contrivance.
- (b) Dissemination of information through the media, including the Internet, or by any other means, which gives, or is likely to give, false or misleading signals as to the supply, demand or price of financial instruments, including the dissemination of rumours and false or misleading news.

3. 'Financial instrument' shall mean instruments listed in Section A of the Annex.

4. 'Regulated market' shall mean a market as defined by Article 1(13) of Directive 93/22/EEC<sup>(1)</sup>.

5. The definitions referred to in this Article and Section A of the Annex shall in order to take account of technical developments on financial markets and to ensure uniform application in the Community of this Directive be clarified and adapted by the Commission in accordance with the procedure referred to in Article 17(2).

#### Article 2

1. Member States shall prohibit any natural or legal person who possesses inside information from taking advantage of that information by acquiring or disposing of it for his own account or for the account of a third party, either directly or indirectly, financial instruments to which that information relates.

The first subparagraph shall apply regardless of whether such person has obtained that information:

- (a) by virtue of his membership of the administrative, management or supervisory bodies of the issuer, or
- (b) by virtue of his holding in the capital of the issuer, or
- (c) by virtue of his having access to the information through the exercise of his employment, profession or duties.

2. Where the person referred to in paragraph 1 is a company or other type of legal person, the prohibition laid down in that paragraph shall also apply to the natural persons who take part in the decision to carry out the transaction for the account of the legal person concerned.

3. The prohibition laid down in paragraph 1 shall apply to any acquisition or disposal of financial instruments.

#### Article 3

Member States shall prohibit any person subject to the prohibition laid down in Article 2 who possesses inside information from:

- (a) disclosing that inside information to any third party unless such disclosure is made in the normal course of the exercise of his employment, profession or duties;
- (b) recommending or procuring a third party, on the basis of that inside information, to acquire or dispose of financial instruments to which that information relates.

#### Article 4

Member States shall also impose the prohibitions provided for in Articles 2 and 3 on any person other than those persons referred to in those Articles who with full knowledge of the facts possesses inside information.

#### Article 5

Member States shall prohibit any natural or legal person from engaging in market manipulation.

A non-exhaustive list of typical methods used for market manipulation is laid down in Section B of the Annex. The Commission shall adopt, in accordance with the procedure referred to in Article 17(2), amendments of the examples of these methods.

Member States may decide to introduce specific provisions to cover persons acting for journalistic purposes in the normal course of the exercise of their profession.

#### Article 6

1. Member States shall ensure that issuers of financial instruments inform the public as soon as possible of inside information.

2. Member States shall require that whenever an issuer, or a person acting on its behalf, discloses any inside information to any third party in the normal exercise of his employment, profession or duties, as referred to in Article 3(a), it must make complete and effective public disclosure of that information, simultaneously in the case of an intentional disclosure, promptly in the case of a non-intentional disclosure.

<sup>(1)</sup> OJ L 141, 11.6.1993, p. 27.

The provisions of the first sub-paragraph shall not apply:

- (a) if the person receiving the information owes a duty of trust or confidence to the issuer, or expressly agrees to maintain the disclosed information in confidence; or
- (b) if the primary business of the entity receiving the information is the issuance of mandatory credit ratings, provided the information is solely for the purpose of developing a credit rating which will be publicly available.

Member States shall require that issuers, or entities acting on their behalf, establish a regularly updated list of those persons working for them and having access to inside information.

3. An issuer may at its own risk delay the public disclosure of particular information such as not to prejudice his legitimate interests provided that such omission would not be likely to mislead the public and that the issuer is able to ensure the confidentiality of this information.

4. Member States shall require that natural and/or legal persons being responsible for the production or dissemination of research or other relevant information to distribution channels or to the public take reasonable care to ensure that information is fairly presented and disclose their interests or indicate conflicts of interest in the financial instruments to which that information relates.

5. Member States shall require that a natural person, or an entity, professionally arranging transactions in financial instruments shall refrain from entering into transactions, and reject orders on behalf of its clients, if it reasonably suspects that a transaction would be based on inside information or would constitute market manipulation.

6. The Commission shall adopt, in accordance with the procedure referred to in Article 17(2), implementing measures on

- the technical modalities of appropriate public disclosure of inside information as referred to in paragraphs 1 and 2,
- the technical modalities of fair presentation of research and other relevant information and the disclosure of particular interests or conflicts of interest as referred to in paragraph 4.

#### Article 7

This Directive shall not apply to transactions carried out in pursuit of monetary, exchange-rate or public debt-management policy by a Member State, by the European System of Central Banks, a national central bank or any other officially designated

body, or by any person acting on their behalf. Member States may extend this exemption to their federated States in respect of the management of their public debt.

#### Article 8

1. The prohibitions of this Directive shall not apply to trading in own shares in 'buy back' programmes nor to the stabilisation of a financial instrument provided such trading is carried out under agreed conditions.

2. The Commission shall determine these technical conditions in accordance with the procedure referred to in Article 17(2).

#### Article 9

The provisions of this Directive shall apply to any financial instrument admitted, or going to be admitted, to trading on a regulated market in at least one Member State, irrespective of whether the transaction itself actually takes place on that market or not.

#### Article 10

Every Member State shall apply the prohibitions and requirements provided for in this Directive at least to actions undertaken within its territory whenever the financial instruments concerned are admitted, or going to be admitted, to trading in a Member State.

#### Article 11

Every Member State shall designate a single administrative authority competent to ensure that the provisions of this Directive are applied.

#### Article 12

The competent authority shall be given all supervisory and investigatory powers that are necessary for the exercise of its functions. It shall exercise such powers either directly or, where appropriate, in collaboration with other authorities, including judicial authorities.

These powers shall include at least the right to:

- (a) have access to any document and to receive a copy of it;
- (b) demand information from any person, and if needed, to require the testimony of a person;
- (c) carry out on-site inspections;

- (d) require telephone and data traffic records;
- (e) request the freezing and/or the sequestration of assets;
- (f) request temporary prohibition of professional activity.

The first and second paragraphs shall be without prejudice to national legal provisions on professional secrecy.

#### Article 13

Member States shall provide that all persons who work or who have worked for the competent authority, as well as auditors and experts instructed by the competent authority, shall be bound by the obligation of professional secrecy. Information covered by professional secrecy may not be divulged to any person or authority except by virtue of provisions laid down by law.

#### Article 14

1. Member States shall ensure that the appropriate measures be taken, including of administrative and criminal sanctions in conformity with their national law, against the natural or legal persons responsible where the provisions of this Directive have not been complied with. Member States shall ensure that these measures are effective, proportionate and dissuasive.

2. Member States shall determine the sanctions to be applied for failure to co-operate in an investigation subject to Article 12.

3. Member States shall provide that the competent authority may disclose to the public every sanction that will be imposed for infringement of the measures taken pursuant to this Directive, unless the disclosure would jeopardise the financial markets or cause disproportionate damage to the parties involved.

#### Article 15

Member States shall ensure that the decisions taken by the competent authority may be subject to the right to apply to the courts.

#### Article 16

1. Competent authorities of Member States shall co-operate with each other whenever necessary for the purpose of carrying out their duties, making use of their powers, whether set out in this Directive or in national law. Competent authorities shall render assistance to competent authorities of other Member States. In particular, they shall exchange information and co-operate in investigation activities.

2. Competent authorities shall, on request, immediately supply any information required for the purpose referred to in paragraph 1. Where necessary, the competent authorities being requested shall immediately take the necessary measures in order to gather the required information. If the requested competent authority is not able to supply the required information immediately it shall notify the requesting Competent Authority of the reasons. Information thus supplied shall be covered by the obligation of professional secrecy to which the persons employed or formerly employed by the competent authorities receiving the information are subject.

The competent authorities may refuse to act on a request for information where communication might adversely affect the sovereignty, security or public policy of the State addressed, or where judicial proceedings have already been initiated in respect of the same actions and against the same persons before the authorities of the State addressed or where final judgment has already been passed on such persons for the same actions by the competent authorities of the State addressed.

Without prejudice to the obligations to which they are subject in judicial proceedings under criminal law, the authorities which receive information pursuant to paragraph 1 may use it only for the exercise of their functions within the scope of this Directive and in the context of administrative or judicial proceedings specifically related to the exercise of those functions. However, where the competent authority communicating information consents thereto, the authority receiving the information may use it for other purposes or forward it to other States' competent authorities.

3. Where a competent authority is convinced that activities contrary to the provisions of this Directive are being or have been carried out on the territory of another Member State, it shall notify this in as specific a manner as possible to the competent authority of the other Member State. The competent authority of the other Member State shall take appropriate action. It shall inform the notifying competent authority of the outcome and, to the extent possible, of significant interim developments.

4. A competent authority of one Member State may request that an investigation be carried out by the competent authority of another Member State, on the latter's territory.

It may further request that some of its own personnel be allowed to accompany the personnel of the competent authority of that other Member State during the course of the investigation.

The investigation shall, however, throughout be subject to the overall control of the Member State on whose territory it is conducted.

The competent authorities may refuse to act on a request for carrying out an investigation as provided for in the first subparagraph of this paragraph, or on a request for its personnel to be accompanied by another Member State competent authority personnel as provided for in the second subparagraph of this paragraph, where such an investigation might adversely affect the sovereignty, security or public policy of the State addressed, or where judicial proceedings have already been initiated in respect of the same actions and against the same persons before the authorities of the State addressed or where final judgment has already been passed on such persons for the same actions by the competent authorities of the State addressed.

5. The Commission shall adopt, in accordance with the procedure referred to in Article 17(2), implementing measures on the procedures of exchange of information and cross-border inspections as referred to in this Article.

#### Article 17

1. The Commission shall be assisted by the European Securities Committee instituted by Commission Decision (2001/. . ./EC) <sup>(1)</sup>.

2. Where reference is made to this paragraph, the regulatory procedure laid down in Article 5 of Decision 1999/468/EC shall apply in compliance with Article 7 and Article 8 thereof.

<sup>(1)</sup> Commission Decision establishing the European Securities Committee, not yet adopted.

3. The period provided for in Article 5(6) of Decision 1999/468/EC shall be three months.

#### Article 18

Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive the (year, month, day: not later than one year after the entry into force of this Directive). They shall forthwith inform the Commission thereof.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

#### Article 19

Directive 89/592/EEC is repealed with effect from the date shown in Article 20.

#### Article 20

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Communities*.

#### Article 21

This Directive is addressed to the Member States.

## ANNEX

### SECTION A

#### Financial Instruments

'Financial Instrument' shall mean:

- Transferable securities as defined in Directive 93/22/EEC
- Units in collective investment undertakings
- Money-market instruments
- Financial-futures contracts, including equivalent cash-settled instruments
- Forward interest-rate agreements
- Interest-rate, currency and equity swaps
- Options to acquire or dispose of any instrument falling in these categories, including equivalent cash-settled instruments. This category includes in particular options on currency and on interest rates
- Derivatives on commodities.

## SECTION B

**The following illustrative examples of methods being used for market manipulation are not exhaustive, but shall serve the interpretation of the general definition provided by Article 1(2):**

- Trade-based actions intended to create a false impression of activity:
    - Transactions in which there is no genuine change in actual ownership of the financial instruments ('Wash sales');
    - Transactions where both buy and sell orders are entered at the same time, with the same price and quantity by different, but colluding parties ('improper Matched orders');
    - Engaging in a series of transactions that are reported on a public display facility to give the impression of activity or price movement in a financial instrument ('Painting the tape');
    - Engaging in an activity designed by a person or persons acting in collaboration to push the price of a financial instrument to an artificially high level (pumping the financial instruments on the market) and then to sell its or their own financial instruments massively ('Pumping and dumping');
    - Increasing the bid for a financial instrument to increase its price (creating the impression of strength or the illusion that stock activity was causing the increase). ('Advancing the bid');
  - Trade-based actions intended to create a shortage:
    - Securing such a control of the bid or demand-side of the derivative and/or the underlying asset that the manipulator has a dominant position which can be exploited to manipulate the price of the derivative and/or the underlying asset ('Cornering');
    - Like 'cornering' taking advantage of a shortage in an asset by controlling the demand-side and exploiting market congestion during such shortages in such a way as to create artificial prices. Having significant influence over supply or delivery, having the right to require delivery and using that to dictate arbitrary and abnormal prices ('Abusive squeezes');
  - Time-specific trade-based actions:
    - Buying or selling financial instruments at the close of the market in an effort to alter the closing price of the financial instrument and therefore misleading those acting on the basis of closing prices ('Marking the close');
    - Trading specifically to interfere with the spot or settlement price of derivative contracts;
    - Trading to influence the particular spot price for a financial instrument that had been agreed as determining the value of a transaction;
  - Information-related actions:
    - Purchasing a financial instrument for one's own account before recommending it to others and then selling it at a profit on the rise in the price following the recommendation ('Scalping');
    - Spreading false rumours to induce buying or selling by others;
    - Making untrue statements of material facts;
    - Non-disclosure of material facts or material interests.
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