

Market Abuse Regulation - Are you ready?



Background

In 1989 the EEC enacted a Directive prohibiting Insider Dealing. Up to that point only three of the then twelve Member States had a statutory prohibition of the practice.

27 years on and the insider dealing regime has developed significantly, and the next step in the EU's move to clamp down on this practice will come on 3 July 2016 when the EU Market Abuse Regulation (MAR) and the Criminal Sanctions Directive for Market Abuse (CSMAD) come into effect.

MAR will replace the existing Market Abuse Directive (2003/6/EC) – generally known as the '2003 Directive'. It takes immediate binding legal effect on 3 July, and will require Ireland to enhance its existing Regulations to give full effect to the regime.

CSMAD will complement MAR and will require all Member States to provide for harmonised criminal market abuse offences, such as insider trading, market manipulation and the manipulation of benchmarks. It provides for maximum prison terms of not less than four years for insider dealing and market manipulation and not less than two years for unlawful disclosure of inside information.

The key features of MAR

The primary aims of MAR are to ensure the integrity of financial markets and to maximise investor protection across Europe through a combination of new requirements and enhancements to the existing regime. These changes also seek to address some of the shortcomings identified with the regime during the financial crisis, such as the absence of an offence of attempted market manipulation, which is now included in MAR.

MAR will extend the current regime beyond financial instruments traded on EU regulated markets to include instruments traded on:

- Multilateral trading facilities (MTF) i.e. a non-exchange financial trading venue
- Organised trading facilities (OTF) i.e. a multilateral system which is not a regulated market or MTF and in which multiple third party buying and selling interests instruments are able to interact in the system in a way which results in a contract
- Over the counter (OTC) i.e. where trading is done directly between two parties, without any supervision of an exchange.

MAR will still apply to market participants such as issuers of financial instruments, investment firms, credit institutions, market operators and persons professionally arranging transactions in those financial instruments.

While the definitions of inside information, insider dealing and market manipulation are largely unchanged, MAR includes other definitions, which were previously set out in delegated legislation, such as:

- “Information of a precise nature”
- “Significant effect on price”
- “Reasonable investor test.”

MAR also encapsulates market abuse across commodity and related derivative markets, and explicitly bans the manipulation of benchmarks (such as LIBOR). The new regime also seeks to ensure that regulations keep pace with the growing trend towards the use of algorithmic and high frequency trading (‘HFT’).

The new Regulation will be underpinned by delegated legislation based on binding technical standards and guidelines developed by ESMA. These so-called “Level II” measures are designed to improve the quality of information available to investors and competent authorities by setting out prescriptive formats for insider lists, Persons Discharging Managerial Responsibility (PDMR) disclosures and the reporting of suspicious transactions and orders.

So what are the key changes from the current market abuse regime?

Insider Lists

The existing requirement for issuers of instruments to maintain an insider list comprised of employees and advisers who are in possession of inside information has been enhanced. In future, the content and form of insider lists will be set out more prescriptively with the aim of establishing a harmonised standard across all Member States.

Insider lists will include personal details of insiders – date of birth, national identification number, addresses, telephone numbers etc and also the date and time and the reason that the individual has been included on the insider list.

Significantly, MAR codifies the decision of the Court of Justice of the European Union in the so-called “Spector Photo” case. Thus confirming, that a rebuttable presumption is placed on a person in possession of inside information to prove that they did not in fact use that information when they traded. Accordingly, the insider list will be central to any enforcement actions and as such accuracy of same will be crucial.

PDMRs

MAR includes an explicit trading ban imposed on PDMRs during “closed periods” – defined as 30 calendar days before the publication of half-year and full-year financial reports. There are a number of very limited prescribed circumstances (e.g. personal hardship) where this trading ban can be lifted.

MAR retains the section of the 2003 Directive requiring PDMRs and persons closely associated to them such as their spouse or dependent children to disclose transactions to the market. The *de minimis* threshold of €5,000 in a calendar year continues to apply although Member States have discretion to increase the *de minimis* threshold to €20,000.

Market Soundings

First of all it might be useful to define what exactly “market soundings” are. This is a commonly-used definition: “A communication of information, before the announcement of a transaction, aiming to gauge the interest of potential investor(s) in a transaction.”

MAR introduces new provisions covering the disclosure of inside information in the course of market soundings. For the disclosure of such information to be considered legitimate, a number of detailed record-keeping requirements must be satisfied. These include the consent of the proposed recipient to receive the relevant insider information and also communication of the restrictions imposed on them once they have received this information. The requirement to notify the recipient that the information in question no longer constitutes inside information could pose considerable challenges in practice.

Suspicious Transaction and Order Reports (STORs)

MAR considerably extends the scope of the requirement to report suspicious transactions to the competent authority. The reporting requirement now extends to suspicious orders, modification to and/or cancellation of transactions or orders and OTC derivative transactions and orders.

MAR also requires market operators, investment firms and persons professionally arranging or executing transactions (which could include AIFMs, UCITS Managers, proprietary traders and those engaged in algorithmic trading as defined in MiFID II) to establish and maintain effective systems and procedures to prevent and detect actual or attempted market abuse and to report same to the competent authority without delay.

Investigative Powers for National Competent Authorities

MAR includes various provisions which ensure competent authorities have minimum investigative and enforcement

powers to combat market abuse. These powers are quite extensive, and include access to premises, access to data traffic and telephone records held by investment firms and telecom operators, in accordance with national law and to request the freezing or sequestration of assets. MAR also requires Member States to provide for the protection of “whistle-blowers” and accused persons.

Sanctions - Fines & Disgorgement of Profits

MAR will also introduce more harmonised administrative sanctions for individuals or corporations found guilty of market abuse, including disgorgement of profits made/ losses avoided, withdrawal or suspension of the authorization of an investment firm or the imposition of a ban on an individual held responsible for the infringement, from exercising management functions in investment firms.

Fines for individuals found guilty of the most serious market abuse offences of insider dealing, unlawful disclosure or market manipulation carry a maximum penalty of at least €5 million.

For corporations, the potential penalties are more severe – a maximum fine of at least €15 million or 15% of annual turnover for insider dealing, unlawful disclosure and market manipulation.

Regulators will have discretion to take account of mitigating or aggravating circumstances, such as the gravity of the offence, previous offences or a suspect’s cooperation with an investigation.

How KPMG can help

Market participants, subject to MAR, need to revise and update their policies and procedures, particularly with respect to the control and disclosure of inside information, monitoring of share dealings by senior executives and maintenance of insider lists.

KPMG can assist market participants to:

- Review and update policies, procedures and controls on the handling of inside information both internally and when publication is required
- Assess the impact of the enhanced requirements on investment recommendations, including reviewing communications sent by advisors to clients and investors, from research notes to television and radio broadcasts
- Revise insider lists and trading policies to ensure that they are reflective of the new requirements in MAR
- Review IT requirements for the collection and storage of transaction and telephone recording data
- Provide training and awareness programmes to ensure that employees, PDMRs and closely associated persons are aware of their obligations under the new market abuse regime, and sanctions for breaches of those obligations.

Contact us

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Produced by: KPMG’s Creative Services. Publication Date: June 2016 (1885)