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INTERPRETATION OF THE MARKET ABUSE REGULATION - ISSUES & SOLUTIONS FINAL

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INTRODUCTION

The protracted legislative process that led to MAR's adoption illustrates the scope and complexity of this comprehensive reform. ESMA's Q&A may help to clarify supervisory practices for issuers across Europe. Nevertheless, certain ambiguities remain. With this paper, EuropeanIssuers would like to draw attention of ESMA and the National Competent Authorities to certain issues of high importance where clarifications could prevent listed companies from unnecessary burdens.

While we welcome supervisory convergence, ensuring that EU legislation is implemented in all Member States as consistently as possible, we caution against guidance on certain MAR provisions which is not clear in terms of regulatory objectives. Therefore, with the following proposals clarifying certain MAR provisions, we attempt to ensure legal certainty needed by stakeholders.

ISSUES & SOLUTIONS

1. CLOSELY ASSOCIATED LEGAL PERSONS – MAR Art. 3 par. 1 (26) (d)

Art. 19 of MAR on Managers' transactions, requires issuers' managers and persons closely associated with them to notify the issuer and the National Competent Authority (NCA) of their transactions relating to said issuer's shares, debt instruments, derivatives or other financial instruments.[1] The transactions must be notified promptly and no later than three business days after the date of the transaction.

For the purpose of notifying managers' transactions, Art. 3 par. 1 (26) (d) of MAR defines when "a legal person is considered to be closely associated with a person discharging managerial responsibilities (PDMR):

(a) a spouse, or a partner considered to be equivalent to a spouse in accordance with national law;
(b) a dependent child, in accordance with national law;
(c) a relative who has shared the same household for at least one year on the date of the transaction concerned; or
(d) a legal person, trust or partnership, ***the managerial responsibilities of which are discharged*** *by a person discharging managerial responsibilities or by a person referred to in point (a), (b) or (c), or which is directly or indirectly controlled by such a person, or which is set*

[1] The EC Delegated Regulation includes a list with examples of the types of notifiable transactions.

up for the benefit of such a person, or the economic interests of which are substantially equivalent to those of such a person."

This definition in this Article is almost the same as in the Directive 2004/72/EC.

However, in the course of implementing the requirements for managers' transactions, it is of utmost importance to confirm that transactions carried out by a "legal person closely associated" to a PDMR are required to be notified only when it is reasonable.

Unfortunately, regulators in various Member States appear to have diverging interpretations regarding the scope of the definition and thus guidance appears necessary. The differing interpretations of regulations could be roughly summarized as follows:

- the "**Strict Interpretation**": a legal person will only be considered to be closely associated with a PDMR, if such PDMR has a control position in that legal person and can also secure himself/herself material economic benefit from the transactions under consideration. This appears to be the view of most NCAs and would be in line with the well proven-practice under the Market Abuse Directive (MAD).
- the "**Wide Interpretation**": we hear that few NCAs appear to consider that a legal person is closely associated with a PDMR if the latter could be considered a PDMR in that legal person without requiring any additional condition to be met. For instance, when the PDMR is a director or a senior manager of the legal person.

The following examples illustrate that only a strict interpretation of Art. 3 par. 1 (26) (d) of MAR ensures a reasonable notification practice:

- Issuers' managers (PDMRs) may have mandates in more than one company. For instance, members of a board of an issuer (company A) may have further mandates on boards of other companies (e.g. company B) without having any material economic benefit from transactions undertaken by the company B. In this example, also the influence of the issuers' managers (PDMR) of company B is very limited. It would go much too far, if this kind of cross directorship would affect the companies A and B so that they are regarded as closely associated legal persons and in consequence be obliged to notify any transaction in the financial instruments of the other legal entity. For instance, if the company B was a bank, its entire trading activity in financial instruments of the issuer A would fall under the notification duty, which could result in an extremely high number of notifications. This would result in flooding the market with unnecessary and confusing notifications instead of increasing transparency.
- In the same vain, non-profit entities should not be considered as closely associated legal persons, as a PDMR can clearly not derive any economic benefit from them. A typical case would be when a CEO of a listed company A is also working in an honorary capacity on the board of a non- profit foundation. A wide interpretation of the MAR could here result in two duties: (1) a notification duty of the foundation if it buys shares of the listed company A for asset management reasons; and (2) a duty of the issuer to include the foundation on the list of persons closely associated. This is obviously not in line with the objective of the regime for notifying managers' transactions.

Were the above situations leading to a notification duty, the regime for notifying managers' transaction would lead to absurd results:

- Due to an extremely high number of concerned transactions, their identification and, therefore, their notification risks not being practically feasible;
- The market would be flooded with non-informative and confusing notifications; and
- Legitimate interests of company B (e.g. as to confidentiality) would be disregarded.

We would like to point out that our examples illustrate only situations in which there is only some "link" to the PDMR and the legal person under consideration. However, the same problems would apply to legal persons associated with those natural persons who are closely associated with the PDMR. In such cases, a wide interpretation could lead to even more absurd results.

We therefore ask ESMA to clarify that at least for the circumstances mentioned above, no notification is expected from the legal person in question. The "strict" interpretation has been a well proven practice in several countries and in line with the objective of the European regime for managers' transactions, reflected in the rationale and the wording of the Market Abuse Regulation:

Wording of Art. 3 par. 1 (26) (d) of MAR

- The wording of Art. 3 par. 1 (26) (d) of MAR supports a reasonably strict interpretation pointing towards the PDMR having a significant level of influence on the entity in question. For example, the wording of the English version of Art. 3 par. 1 (26) (d) of MAR supports the "strict interpretation": *"a legal person… the managerial responsibilities of which are discharged…"* already implies that the managerial responsibilities are entirely discharged by the PDMR in question. Compared to a "person discharging managerial responsibilities" (see definition in Art. 3.1 (25) of MAR) a manager who discharges the managerial responsibilities of an entity is in charge of the management of this entity.
- If the intention of the European co-legislators had been to include any legal person in which the PDMR technically discharges managerial responsibilities as a closely associated legal person, the wording would have clearly referred to any legal person in which the PDMR of entity A is also a PDMR of entity B, irrespective of whether there is real control over the legal entity or a personal economic benefit from transactions undertaken by that legal person. They would have clearly stated that any legal person in which the PDMR was also a PDMR would be considered as a closely associated person.

Rationale of Art. 3 par. 1 (26) (d) of MAR

- The objective of Art. 3 par. 1 (26) of MAR has always been to avoid the circumvention of notification duties by using a vehicle or strategy that allows the manager (PDMR) and / or person closely associated to benefit from the transaction without a notification. The only incentive for such behaviour is a potential material economic benefit. A meaningful threshold for defining a material economic benefit would be at least 50% of earnings (in dividends and / or other forms of remuneration). Therefore, we understand that the European co-legislators intended to address situations when a manager (PDMR) has 'control' and is able to derive a material personal economic benefit from the transaction undertaken by the company. Examples include: a) associations via 'family' links (i.e. spouse, partner, dependent child or those living with him) and b) in the case of legal entities, either, by controlling its management (discharging *the* managerial responsibilities), by controlling its property; or simply because the

legal entity was set up for his personal benefit. None of those the examples on page 3 could result in such circumvention.

- Furthermore, the publication of transactions mentioned in the examples on page 3 would neither prevent market abuse or insider dealing, nor would it be a valuable source of information to investors (see recital 58 of MAR). It would neither be helpful for the NCAs to supervise markets (see recital 59 of MAR). It also would not serve the objective of Art. 19 MAR which is to inform the market whether expectations of the person discharging managerial responsibility at the issuer have changed regarding the future development and performance of the issuer's shares.

We would like to highlight that the "strict approach" is not only in line with the supervisory practices under the previous Market Abuse Directive, but also reflected in the most recent guidance: see the preliminary view of the German BaFin Q&A, the City of London Law Society and Law Society Company Committees' Joint Working Group Parties which recalls an interpretation of the UK FSA in 2005).

Concluding, it is of utmost importance to the issuers all over Europe that a "strict interpretation" is applied in cases described on page 3. Such approach would ensure adequate transparency while providing for a reasonable and feasible approach for managers' transactions. We count on ESMA in that respect to help align supervisory practices in a sensible and coherent manner.

2. PERSONS PROFESSIONALLY ARRANGING OR EXECUTING TRANSACTIONS - Art. 16 par. 2

Art. 16 par. 2 of MAR states: "*Any person professionally arranging or executing transactions shall establish and maintain effective arrangements, systems and procedures to detect and report suspicious orders and transactions*".

According to Art. 3 par. 1 (28) "a person professionally arranging or executing transactions means *"a person professionally engaged in the reception and transmission of orders for, or in the execution of transactions in, financial instruments*".

EuropeanIssuers understands that the purpose of the Q&A on MAR published by ESMA in May 2016[2] is to clarify that the definition of a person professionally arranging or executing transactions not only catches investment firms but also investment management firms and other entities engaged in proprietary trading on professional basis. Thus, ESMA clarified that if obtaining revenue from trading in financial instruments is the core part of the firm's business model, such a firm is within the scope of Art. 16 par. 2 of MAR.

Against this background, we consider that Art. 16 par. 2 does not apply to non-financial companies (NFCs) whose business is focused on production of goods and / or services and not arranging or executing financial transactions. NFCs, representing the "real economy", engage in financial transactions on ancillary basis, for instance to hedge the market and price related risks resulting from their operations. Moreover, in the respective transactions, NFCs act as clients of the financial sector, not as providers of financial services or market makers.

[2] Questions and Answers on the Market Abuse Regulation (ESMA/2016/1520)
https://www.esma.europa.eu/sites/default/files/library/2016-1520_mar_qa.pdf

Therefore, unless the transactions are carried out by a subsidiary that is already a regulated entity authorized to deliver proprietary trading, investment or asset management services, NFC should not be obliged to comply with the obligation to report suspicious orders and transactions. This would not bring any benefit in practice as NFCs enter into financial transactions due to operational requirements, and not to use markets for financial gains.

It is our understanding that the ESMA Q&A published in May 2016 on that issue should be interpreted in this sense. ESMA mentions only the market participants for whom financial markets activities are core to their business model, be it because they are a specific class of intermediaries (e.g. Alternative Investment Funds) or because proprietary trading is their main business. None of these criteria applies to NFCs.

We would therefore ask ESMA to clarify this aspect through an amendment to the existing Q&A that NFCs, as described above, are not covered by Art. 16 par. 2 of MAR. To our knowledge currently the supervisory practices across the EU are not harmonized on that issue. While it is important to avoid legal uncertainty, additional compliance cost and risks for European non-financial companies across Europe. Otherwise, there is a risk that non-financial companies would have to implement a kind of Suspicious Transaction & Order Reporting (STOR), which surely has not been the intention of the co-legislators.

3. INSIDER LISTS – Art. 18

Art. 18 of MAR stipulates:

"1. Issuers or any person acting on their behalf or on their account, shall:

(a) draw up a list of all persons who have access to inside information and who are working for them under a contract of employment, or otherwise performing tasks through which they have access to inside information, such as advisers, accountants or credit rating agencies (insider list);

(b) promptly update the insider list in accordance with paragraph 4; and

(c) provide the insider list to the competent authority as soon as possible upon its request.

2. Issuers or any person acting on their behalf or on their account, shall take all reasonable steps to ensure that any person on the insider list acknowledges in writing the legal and regulatory duties entailed and is aware of the sanctions applicable to insider dealing and unlawful disclosure of inside information.

Where another person acting on behalf or on the account of the issuer assumes the task of drawing up and updating the insider list, the issuer remains fully responsible for complying with this Article. The issuer shall always retain a right of access to the insider list."

To ensure regulatory certainty and consistency of the common practice, we believe that Art. 18 par. 2 should be distinguished from Art. 18 par. 1 of MAR.

The latter refers to the third parties such as bankers, lawyers, accountants, etc. working for the issuer on a specific transaction or project and therefore obliged to draw up their own insider lists (with all staff having access to the respective inside information). These third parties are responsible for their own lists. This is the current regulatory practice in several jurisdictions.

On the other hand, Art. 18 par. 2 of MAR allows the issuer to delegate the task of drawing up and updating the list to a third person / service provider acting on the issuer's behalf or account. This

person / service provider, is often engaged by the issuer with the sole purpose to assume the obligation to set up and maintain the issuers' insider list and is not involved in the transaction linked to inside information.

Therefore, we kindly ask ESMA to clarify that third parties working for the issuer on a specific transaction or project shall draw up their own insider lists (listing all the employees having access to the respective inside information) and are responsible for these lists, as it is a current regulatory practice in several jurisdictions. This clarification would increase legal certainty of the common practice of many listed issuers that in their insider list indicate the necessary details of one reference person (working for the third party / service provider) able to identify the persons within that company (third party) having had access to inside information.

4. SME Growth Markets

Art. 18 par. 6 of MAR exempts issuers on SME Growth Markets from producing an insider list. This is a measure that we welcomed since we believe the general requirement to produce and keep insider lists is too onerous for small and mid-size quoted companies.

However, "SME Growth Markets" are defined in MiFID II (Directive 2014/65/EU), which is expected to come into effect in January 2018.

Given that MAR is applicable as of July 2016, this means that, unless any measure is taken, companies quoted on markets which will eventually become SME Growth Markets will have to start keeping insider lists from that date subject to the full requirements of Art. 18.

We urge the Commission and ESMA to assess how this issue can be solved through an exceptional derogation during the interim period between the entry into force of MAR and the application of SME Growth Markets rules to growth markets across the EU. To remedy the current situation, we propose two possible regulatory solutions which could be relatively simple to put in place and would have the full support of smaller companies while achieving the purpose set in MAR:

- Support the NCAs to produce a statement of no action, in which each NCA would state their intention not to prosecute any breaches to the requirement to produce and maintain insider lists by SME issuers on MTFs with a primary market function, if the list is produced upon request by the NCA; or
- Require all companies on an MTF with a primary market function to produce a statement informing their NCA of their intention to comply with the lighter regime set out in MAR for SME Growth Markets.

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EuropeanIssuers *is a pan-European organisation representing the interests of publicly quoted companies across Europe to the EU Institutions. As at 31 December 2014, there were 13 225 such companies on both the main regulated markets and the alternative exchange-regulated markets. Our members include both national associations and companies from all sectors in 14 European countries, covering markets worth € 7.6 trillion market capitalisation with approximately 8000 companies.*

We aim to ensure that EU policy creates an environment in which companies can raise capital through the public markets and can deliver growth over the longer-term. We seek capital markets that serve the interests of their end users, including issuers.

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