PROPOSALS FOR A DIRECTIVE AND A REGULATION OF THE EUROPEAN COMMISSION ON INSIDER DEALING AND MARKET MANIPULATION: CCBE COMMENTS

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The Council of Bars and Law Societies of Europe (CCBE) is the representative organisation of around 1 million European lawyers through its member bars and law societies from 31 full member countries, and 11 further associate and observer countries.

The CCBE has the following comments on the draft directive and regulation:

A. Inside Information

Article 6 Inside Information

The CCBE is concerned that the extended definition of inside information in Article 6.1(e) and Article 6.3 will create problems for listed issuers and investors and impede the good engagement between them that is needed for good corporate governance.

For the purpose of insider dealing etc, information will be inside information (under Article 6.1(e)) if it is not generally available to the public but, if it were available to a reasonable investor who regularly deals on the market would be regarded as "relevant" when deciding the terms on which the transaction is effected. There is no requirement that the information must be likely to change the price at which someone would deal, as well as no requirement for the information to be "precise".

This could inhibit discussions between a listed company and its shareholders. If, for example, the chairman of a company visits a major shareholder as part of the normal investor relations programme, he may know that new production equipment is being installed in one of the company's factories. If the company announced this, it would not move its share price. However, it might still be information the market would regard as relevant when deciding the terms of a transaction (even if it only confirms the basis on which the investor would deal). If so, if the chairman (who is an insider) discloses the information to the investor he may either be improperly disclosing inside information or even inducing the shareholder to deal. He will make the shareholder an insider - who cannot deal unless the information is made "generally available". If listed companies have to announce information that is not price sensitive generally, that would increase significantly the information that companies have to announce and make it harder for investors to identify the relevant price sensitive information.

Similar problems could arise if a major shareholder wanted to discuss a listed company's strategy with it, even if the information to be discussed is not price sensitive or if the company has information about its trading position that is not likely to have a significant effect on price e.g. it has won some new contracts, none of which is material and which together are not material. The listed company would not be able to disclose this to the shareholder as part of a general discussion on current performance with investors, because it could be regarded as relevant.

The proposed wording would also create problems for company employees who want to deal in the company's shares. It would be very difficult - and perhaps impossible - for the company to be sure that the employees do not have information that is relevant but has not been made generally available and so give the employees permission to deal.

The explanatory memorandum says that the reason for the change in approach is because the inside information may not be sufficiently precise for the issuer to have come under an obligation to announce it - rather than the problem being one of price sensitivity. It says that dealings should be prohibited where there is uncertainty about information, either whether a future event will happen or about the effect of publication of that information on the price of the securities affected. However, the drafting of the Regulation does not achieve that aim.

The CCBE believes that the requirement for information to be price sensitive should be retained (as is the case under the current Directive). We believe that the difficulty about whether information is

"precise" can be better dealt with in a different way by looking at the definition of when information is of a precise nature (see Article 6.2).

The change in the definition of inside information made by Article 6.3 will also cause problems for listed issuers in deciding what information they must announce.

At present, for the announcement obligation to arise the information must be both (i) likely to have a significant effect on the price of the affected financial instruments and (ii) be information a reasonable investor would be likely to use as part of the basis of his investment decision. The proposed change in Article 6.3 of the Regulation means that if information is information a reasonable investor would be likely to use as part of the basis of his investment decision, it is deemed to be information that would be likely to have a significant effect on the price of the financial instrument (even if, in practice it would not affect the price).

Unless this is changed, listed companies will in practice find it almost impossible to decide what information they should announce, as most of the information they have could be information a reasonable investor would be likely to use as part of the basis of his investment decision. Although issuers can rely on the ability to delay the announcement of information where it is still subject to negotiation (e.g. negotiation of a contract or an acquisition or disposal), there will be large amounts of information the company has which are not subject to negotiation and will therefore have to be announced. Again, the result of this would be to make so much information announceable as to be unhelpful for investors.

Lack of defences for insider dealing

Many of the recitals in the Market Abuse Directive do not appear in the Regulation. These are very important in defining the scope of the insider dealing offence. They include Recital 29 (using inside information in the context of a takeover) and Recital 30 (dealing on one's own intentions). They (and other defences in the Directive) should be replicated in the Regulation.

Use of inside information – Spector Photo case[1]

In the Spector Photo case the ECJ held that once the elements of insider dealing are present it may be assumed that the person dealing intended to deal on the basis of the inside information. It is not necessary to prove that the inside information influenced the decision to deal. However, it said this could lead to injustice and there may be defences that could be used in some cases.

The Regulation creates an express defence for persons who put in place effective Chinese Walls but does not refer to other defences that might be available. It therefore undermines the comfort that the Spector case would otherwise provide. We believe the Regulation should make it clear that insider dealing will not be committed if the inside information does not materially influence the decision to deal.

Proposal for a Directive of the European Parliament and of the Council on criminal sanctions for insider dealing and market manipulation

Article 7 sets out when a legal person is to be held to commit a criminal offence. We think the proposed wording is unclear when it refers to "any person who has a leading position… either individually or as part of an organ". We also think that "lack of supervision or control" is not an appropriate basis on which to impose criminal liability. It is not clear what an individual is expected to do to supervise or control the person who commits the offence – and therefore what the failure is which gives rise to the liability.

1 Spector Photo Group NV, Chris Van Raemdonck v Commissie voor het Bank, Financie-en Assurantiewezen (CBFA) c-45/08).

B. Accumulation of administrative and criminal sanctions

The proposed Directive published by the European Commission on 20 October 2011 aims to establish, within each Member state, a criminal penalty for stock market offences - insider dealing and market manipulation.

Since actions taken against market abuse can vary substantially from one Member state to another, the European Commission aims, through this Directive, to ensure minimum criminal sanctions throughout the EU.

Insider dealing and market manipulation, as well as incitement to commit such offences, and complicity, are covered.

Of course, this proposal is in the interest of the market: market abuses, like markets themselves, can be cross-border issues. Any bad behaviour in financial markets should be sanctioned, ensuring the offender cannot take advantage of the lack of enforcement in this area in the state where the offence is committed.

Therefore, the CCBE welcomes the initiative from the European Commission to strengthen market integrity. Harmonising at European level the principle that market abuses must be punished will have a deterrent effect and will strengthen the system set up by the Market Abuse Directive in 2003.

However, the CCBE regrets that the draft Directive does not address the issue of the accumulation of criminal and administrative sanctions for insider dealing and market manipulation.

The CCBE, in order to guarantee the rights of defence, is deeply committed to the idea that the *double jeopardy* principle should be respected and that a person cannot be punished twice for the same offence. This may be the case where a state has established both administrative and criminal sanctions to punish the same misconduct on the markets.

In France for instance, the *Autorité des marchés financiers* (AMF) has a power of control, and also a power to impose sanctions on markets for an amount to be paid as fines of up to 100 million Euros. However, despite the double jeopardy principle, the same facts may constitute a criminal offence also subject to a pecuniary sanction and imprisonment. For over 20 years, the issue of the accumulation of both administrative and criminal sanctions has been debated in France. Many discussions and reports have taken place, including the report of the working group chaired by Jean-Marie Coulon, which called for the co-operation of administrative and criminal teams for the sanction of market misconduct.

The solution put forward by the AMF to have no double jeopardy when criminal offences are committed intentionally, as opposed to the violations they sanction, seems artificial.

It should also be noted that the proposed Directive retains intent as an element of the criminal offence. But how could insider dealing, market manipulation or incitement to commit a market offence be unintentional?

If criminal sanctions were imposed in all Member states, these situations will probably grow in number.

In its decision of 10 February 2009 (*Zolotukhin v. Russia*), the Grand Chamber of the European Court of Human Rights found that, when there was accumulation of both administrative and criminal sanctions, there was a violation of Article 4 of Protocol 7 under which '*No one shall be liable to be tried or punished again in criminal proceedings under the jurisdiction of the same State for an offence for which he has already been finally acquitted or convicted in accordance with the law and penal procedure of that State*'.

It therefore seems paramount to put an end to situations where the same conduct on the market may be sanctioned by both the regulatory authorities and by the criminal court.

Such need makes all the more sense in terms of the proposal for a Regulation on insider dealing and market manipulation, also released on 20 October 2011. This Regulation of direct application would strengthen the powers of regulators. On the one hand, the regulators would see their field of intervention extended to multilateral trading platforms, to over-the-counter markets as well as energy and raw materials. On the other hand, a broadening of the definition of 'inside information' is proposed.

Based on these new powers, competent judicial and/or administrative authorities will increase their activity and there is concern that this increased power of control may bring along many disputes and repeated violations of the double jeopardy principle.

It is therefore in the interest of the market and administrative and judicial authorities to seize the opportunity of these proposals for a Directive and a Regulation to stop the accumulation of both administrative and criminal sanctions relating to market offences.

In this regard, the CCBE notes that Article 26 of the Regulation enumerates 13 administrative measures and sanctions for insider dealing and market manipulation. 10 of these measures, i.e. from (a) to (j), are supervisory measures, which would best be implemented by regulators: injunction to stop misconduct, public statement, correcting false or misleading information, temporary activity ban, withdrawal of approval, freezing of assets, etc.

However, the measures set out in Article 26 (k) to (m) of the Regulation are financial sanctions which can be accumulated with a criminal sanction - even more so if a criminal sanction is mandatory in all Member states.

The CCBE is therefore in favour of the removal of issues (k) to (m) from the list of measures and sanctions which can be imposed by administrative authorities.