



COMMITTEE OF EUROPEAN SECURITIES REGULATORS
THE CHAIRMAN

Mr. David Wright
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Internal Market and Services
European Commission
rue de la Loi, 200
1040 Bruxelles,
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RE: CESR's response to the Commission call for evidence on the review of the Market Abuse Directive

Dear David,

CESR has been very active since the entry into force of the Market Abuse Directive (MAD) seeking to contribute in its Level 3 capacity to promoting a harmonised approach amongst securities regulators in the area of surveillance and enforcement of market abuse.

Aiming at facilitating the effective implementation of the new market abuse regime and at ensuring common approach to the directive's operation among securities regulators, CESR has produced three sets of Level 3 guidance which were designed to enhance convergence in supervisory practices and to provide further clarity for market participants regarding the operational requirements and issues with regard to certain particular significant areas of the MAD.

CESR's first set of guidance at Level 3 (CESR/04-505b) published in May 2005 concentrated on the accepted market practices in relation to market manipulation, guidance on what CESR considers to constitute market manipulation and guidance and a common reporting format for submitting suspicious transactions reports – issues highly prioritised by CESR at the time the new market abuse regime was introduced.

In December 2005 CESR agreed that a second phase of market-facing Level 3 work in respect of MAD should be carried out. To facilitate this initiative, an extensive consultation with market participants by the means of the Call for Evidence on "Evaluation of the supervisory functioning of the EU market abuse regime" (CESR/06-078) took place in the middle of 2006, requesting recommendations on the issues on which further guidance were needed and proposals to overcome identified obstacles to the efficient functioning of markets.

Following this exercise a second set of guidance (CESR/06-562b) was published in July 2007 covering the following issues: what constitutes inside information; when is it legitimate to delay the disclosure of inside information; when does information relating to a client's pending orders constitute inside information; insider lists in multiple jurisdictions – proposing a mutual recognition system in this area.

Continuing the efforts to ensure ground for convergent implementation and application of the market abuse regime, CESR also elaborated in the third set of Level 3 guidance (CESR/09-219) in May 2009 its common position on the harmonisation of requirements for insiders' lists; suspicious transactions reports (STRs); stabilisation regime at Level 3 and the aspect of rumours in relation to the notion of inside information.

In addition, CESR was asked by the Commission in March 2007 to assist in setting up, for information purposes, a list of administrative measures and sanctions as well as criminal sanctions under the MAD in the EEA Member States, in order to facilitate greater transparency in the application of the MAD and to facilitate the effective implementation and application of the MAD. The report (CESR/08-099) showed quite a divergence in the amounts of administrative pecuniary



finances available to competent authorities as well as differences in respect of the sanctioning regimes applicable in cases of market abuse.

CESR now welcomes the Commission's initiative to review the MAD and the opportunity it represents to comment on the proposals presented.

CESR has considered all the issues included in the Commission's call for evidence. However, CESR has decided to restrict itself in its response only to those issues where CESR members are in common agreement on the basis that individual CESR members are not precluded from providing their own separate, individual responses to the Commission's call for evidence.

CESR remains at the Commission's disposal to provide further clarification on the responses provided upon request.

Yours sincerely,

A handwritten signature in blue ink, appearing to read 'Eddy Wymeersch', is written in a cursive style.

Eddy Wymeersch



CESR's response to the European Commission's call for evidence on the review of Directive 2003/6/EC (Market Abuse Directive).

CESR welcomes the Commission's proposal to review the operation of the Market Abuse Directive (MAD) and the opportunity to provide its comments on the proposals presented.

CESR has considered all the issues included in the Commission's call for evidence in detail. However, CESR has decided in its response to restrict itself only to those issues where CESR members are in common agreement on the basis that individual CESR members are not precluded from providing their own separate, individual responses to the Commission's consultation.

2 ANALYSIS

2.1 THE SCOPE OF THE MAD

2.1.1 Only regulated markets? (Articles 1(3) and 9 of Directive 2003/6/EC)

Question: Do you consider that the scope of the MAD should go beyond regulated markets? In particular, should it be extended to cover MTFs?

CESR agrees in principle that the expansion of the scope of MAD beyond regulated markets, and in particular, for including multilateral trading facilities (MTFs) takes into consideration the growing importance of these trading venues and the fact that some Member States have already extended at national level the application of MAD not only to regulated markets. Furthermore, such an extension will improve the level playing field between the various trading venues and secure market's integrity.

However, there is not a common position of CESR members as to a general extension of the whole market abuse regime to "non-regulated" markets or as to the extension to all MTFs without distinction. It will be important to consider carefully whether all of the Article 6 provisions (disclosure obligations, insider lists etc.) should be applicable.

2.1.2 What kind of financial instruments should be covered by the MAD, especially in comparison with the MiFID? (Article 1(3) of Directive 2003/6/EC)

Questions: Do you agree with an alignment of the MAD definition of financial instrument to the definition for the same concept provided for in MiFID? Do you think it could be useful to explain in more detail in the MAD what is meant by a financial instrument "whose value depends on another financial instrument" or to list asset classes, such as CFDs and CDS, which belong to this category?

As regards the coverage of financial instruments, CESR considers that the prime consideration is that MAD applies to the necessary range of instruments appropriate for the purposes of ensuring the integrity of financial markets. In general, CESR thinks that it would be acceptable to align the definition of financial instruments in the MAD with that provided for in MiFID and particularly agrees that products such as Credit Default Swaps and Contracts for Difference should be covered under MAD. However, care will need to be taken in relation to the part of the MiFID definition which relates to exotic derivatives, to ensure that if these instruments are to be covered by MAD, they are described in a way that is consistent with the purpose and scope of MAD.

CESR has already concluded that it is important to closely observe the developments on the CDS market and noted that, depending on these developments, it may prove useful to consider amending the MAD, where the wording "whose value depends" may be limiting the ability of regulators to properly monitor markets. New text along the lines of any financial instruments "for which a change in value may cause a change of the value of instruments admitted to trading on a regulated market" may therefore need to be included in the scope.

CESR also shares the views that the alignment of the definition of financial instruments in the MAD with that provided for in MiFID (and a possible change of the wording of Art. 9(2) of MAD) will also provide an equal treatment to prohibitions of market manipulation and insider dealing taking into consideration that at present market manipulation cases may not be sanctioned



under MAD in relation to financial instruments not admitted to trading on a regulated market but the value of which depends on the value of another instrument (which is admitted to trading on a regulated market), whereas insider dealing cases may be sanctioned in relation to such instruments.

2.1.3 The specific case of commodity derivatives markets (Article 1(1) of Directive 2003/6/EC)

Question: Do you see a need for introduction of a market abuse framework for physical markets?

CESR maintains its views as expressed in the common report prepared by CESR and ERGEG, according to which the extension of the scope of the MAD regime to physical products is not recommended, as it does not reflect the needs of the energy markets, whose features would not justify such a solution. A tailor-made market abuse regime (not under the financial services regulation) applicable on physical markets might be a possible way forward. It is also noted that commodity derivatives fall within the scope of the MAD regime if they are admitted to trading on regulated markets.

2.2 INSIDE INFORMATION

2.2.1 Definition of inside information: the general definition (Article 1(1) of Directive 2003/6/EC and Article 1 of Directive 2003/124/EC) and the particular definition for commodity derivatives

Question: Do you share this view as far as insider dealing prohibition is concerned? (see also next point for disclosure of inside information). If not, which concepts would you advise to modify and how?

CESR agrees that it is extremely important that the competent authorities in Member States are able to take effective action against those who abuse markets by misusing information before it has been announced to the market. In this context the definition of information for the prohibition of insider dealing is clearly key. CESR members have worked with the existing definition in sanctioning abuses and, as the Commission notes, CESR has provided Level 3 guidance to clarify the application of the various components of the definition. However, a few CESR members have a different view on whether the current Directive definition provides a fully comprehensive standard for the application of the prohibition on inside dealing.

Question: Do you support an alignment of the inside information definition for commodity derivatives with the general definition of the directive?

CESR recognises that the current definition of inside information in relation to commodity derivatives is less precise than the general definition used in the Directive. CESR acknowledges that it can be difficult to identify the information that is “inside information” in relation to commodity derivatives and that inside information in this context may inevitably not be as precise as information that fits the Article 1 definition. CESR therefore considers that a careful approach will be needed to reviewing the definition of ‘inside information’ and notes, for example, that there could be enforcement issues involved in a change of the definition.

2.2.2 Dissemination of inside information and deferred disclosure mechanism (Article 6 of Directive 2003/6/EC and Article 3 of Directive 2003/124/EC)

2.2.2.1 General obligation of disclosure of inside information

Question: Do you consider that any changes to the definition of inside information for disclosure purposes is necessary?

CESR shares the view that the Level 1 definition of inside information for disclosure purposes should not be changed. However, CESR members have different views on whether the Level 2 definition of information ‘...likely to have a significant effect on the prices of ... financial instruments’ provided in Art. 1(2) of implementing directive 2003/124/EC is appropriate.

CESR agrees that there should be the ability for issuers to delay the disclosure of inside information but firmly supports the principle that it is appropriate that – according to Art. 6(2)



and 6(3) – the decision of delaying disclosure must be immediately revisited and the information disclosed if confidentiality can not be ensured any longer or if such delay would be likely to mislead the public or if leaks occur.

In order to provide more certainty for issuers on legitimate interests that can allow them to delay the disclosure, CESR gave in the Second set of Level 3 guidance some illustrative examples that refer to the two circumstances already set out by Art. 3(1) of implementing directive 2003/124/EC.

Question: Do you agree that the described deficiencies of the deferred disclosure mechanism need to be addressed, possibly by way of amendments to the MAD framework? Do you consider that Level 3 guidance could be sufficient?

CESR emphasises the need to proceed carefully if the mechanism for deferred disclosure of inside information were to be revisited and particularly the exemptions to the obligation were to be broadened. Enabling issuers to defer the disclosure of inside information even when the conditions laid down in Article 6 (2) of the Directive were not met would be a serious matter and should obviously only be considered, if at all, in very limited and defined circumstances.

More widely, CESR recognises that there may be some uncertainty amongst market participants as to what actually constitutes “misleading the public” and CESR is therefore ready to examine possible further Level 3 guidance on the meaning of this condition for deferring disclosure.

Do you agree that the issuer may be exempted from disclosing inside information in situations when that information concerns emergency measures being prepared in case the issuer's financial stability is endangered?

See the answer above.

What are other deficiencies in this area that raise major interpretation / application difficulties? What is the best way to address them?

CESR has not identified issues other than those already mentioned in responding to previous questions.

2.2.2.2 Disclosure duty in commodity derivatives markets

Question: Do you agree with this approach? Can you identify cases where a modification or deletion of the obligation may be undesirable for market integrity?

CESR recognises that these issues might warrant further consideration.

2.2.3 Prohibition of insider dealing (Articles 2, 3 and 4 of Directive 2003/6/EC)

Question: Would you support this approach?

At this stage, CESR shares the view that it is appropriate to wait for the ECJ decision.

2.2.4 Three new tools to help to detect suspicious transactions

2.2.4.1 Insider lists (Article 6(3) of Directive 2003/6/EC and Article 5 of Directive 2004/72/EC)

Question: Do you consider that the obligations to draw up lists of insiders are proportionate?

Due to the low degree of detail of Level 1 and Level 2 provisions, some divergences across EU in the regulation of insider lists exist. Therefore, CESR has been working at Level 3 in order to harmonise as much as possible.

2.2.4.2 Transaction reporting by managers and closely associated persons and subsequent disclosure (Article 6(4) of Directive 2003/6/EC and Article 6 of Directive 2004/72/EC)

Question: Do you see a need for a regulatory action in the above areas? Would you suggest further improvements?



CESR sees that there is a need for regulatory action in this area and will examine this issue further going forward.

2.2.4.3 Reporting of suspicious transactions (Article 6(9) of Directive 2003/6/EC and Article 7(11) of Directive 2004/72/EC)

Question: Do you agree that rules on suspicious transactions reporting do not require modifications?

In general CESR is supportive of the STR regime which has proved a valuable source of market abuse referrals for members. CESR has provided additional clarifications regarding the duty to report suspicious transactions at Level 3, identifying particular signals of suspicious transactions and agreeing on a common format for their reporting.

In CESR's view surveillance of OTC derivatives transactions is considered as key for adequate surveillance of the market. The same arguments justify the need for regulators to be alerted by the persons executing suspicious trades in OTC derivatives on behalf of their clients. There is a need for consistency and for a comprehensive approach by European regulators.

Where competent authorities cannot receive Suspicious Transaction Reports ("STR") on OTC derivative instruments, because local legislation does not permit it, CESR would like to request the European Commission to amend the MAD to make STRs on OTC derivative instruments mandatory.

2.2.5 The competent authorities' right of access to telephone and existing data traffic records (Article 12 of Directive 2003/6/EC)

Question: Do you consider that an amendment of the MAD is necessary?

The power of the competent authorities to require telephone and data traffic records and ultimately to obtain these records is considered among the most important issues for the accomplishment of the investigatory and enforcement tasks of CESR members. Experience has shown that access on data traffic records has been problematic in several Member States. CESR, therefore, strongly supports any necessary amendment of the MAD and/or other Directive(s) so that the uncertainties on the rights of the competent authorities to obtain this data can be removed.

2.3 MARKET MANIPULATION

2.3.1. Definition of market manipulation by transactions/orders to trade (Article 1(2) of Directive 2003/6/EC)

Question: Do you think that the definition of market manipulation should be amended? If this is the case, what elements of the definition should be reconsidered?

While CESR agrees that the current definition of market manipulation is good as far as it goes, it also considers that the definition should be extended so that it explicitly includes the attempt to manipulate the market as behaviour subject to the market abuse regime.

Supervisors may face some difficulties in building up cases for market manipulation stemming from the need to obtain enough pieces of evidence to substantiate the case, which is not always easy due to the complex structures that are sometimes used to manipulate the market and the problems in some cases in demonstrating significant actual impact on the market. CESR considers that some of these difficulties could be avoided by including the attempt to manipulate the market as behaviour against which the competent authority may take actions.

In this context CESR notes that the International Organization of Securities Commissions (IOSCO), an international standards setter of which most of the CESR members are also members, states in a recent document on "Commodity Futures Market"¹: "*Where appropriate, futures market regulators should review their existing statutory and administrative market abuse*

¹ <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD285.pdf> IOSCO Taskforce on Commodity Futures Markets, March 2009

authority to determine whether it adequately allows for the prosecution of attempted manipulation. Parties involved in manipulation often do not succeed with the scheme as it is difficult to influence the price of a derivative contract or underlying asset and it is difficult for regulators to prove perfected manipulation. Regulators should take affirmative steps to request the necessary powers to enforce against attempted manipulation”.

CESR considers that the review of the MAD is a good opportunity to implement into European legislation this recommendation and not only for the futures markets but for any financial instrument subject to the market abuse regime.

2.3.2 Accepted Market Practices (AMP) (Article 1(2)(a) and 1(5) of Directive 2003/6/EC)

Question: Do you consider that the rules on accepted market practices should be amended in the MAD? Do you think there is room for greater convergence among competent authorities in this area?

CESR considers that market abuse regime does not require that an AMP that is present in one European market has to be accepted on all other European markets.

2.3.3 Exemptions for buy-back programmes and stabilisation activities (Article 8 of Directive 2003/6/EC and Commission Regulation 2273/2003)

Question: Do you consider that the safe harbours for buy -back programmes and stabilisation activities should be revisited? Do you think that greater convergence is desirable in the application of the Regulation 2273/2003? What would be the most appropriate way forward in this respect?

CESR considers that currently there are no merits to extend the safe harbour on buy-back programmes and stabilisation to activities other than the ones currently included in the Regulation 2273/2003 and that the application of this Regulation is mostly convergent in the Member States and the inconsistencies that might currently exist will reduce over time. However, a few CESR members have a different view and consider that the safe harbour should be extended to companies that buy and hold shares for future use as means of payment for acquiring shares of another company.

As it is already said in the call for evidence not all buy-back programmes and stabilisation activities should benefit from the safe harbour under the MAD but only those that meet the conditions laid down in Regulation 2273/2003. However, CESR members share the views that even those outside Regulation 2273/2003 are not automatically considered as manipulative and already made it explicit through CESR Level 3 Guidance.

On whether there are different interpretations across Europe regarding the applicability of the stabilisation regime to certain kind of instruments (debt securities), as far as CESR is aware – ESME referred to an isolated case with one competent authority. This case has already been clarified also with market participants. It was not a problem of inconsistency in the application of the stabilisation regime established under the MAD but a peculiarity of a domestic regime for the allocation of debt securities issues. It is also fair to say that the scope of Regulation 2273/2003 addresses mainly stabilisation situations in equity markets providing a less detailed framework for debt stabilisation practices.

On the one mMember State regime issue, in the Third set of CESR’s Guidance and information on the common operation of the MAD that CESR has recently published it is said that: “*Whilst CESR is sympathetic to industry’s concerns, it is anticipated, as part of the current work by CESR-Pol, that the level of inconsistencies between Member States will reduce. It is possible that some discrepancies will remain although it is expected that these will further reduce over time.*”

2.3.4 Short selling

Question: Do you see a need for a comprehensive framework for short selling? If so, should it be addressed in the Market Abuse Directive? What issues should such a regime cover?

Question: Should short sellers be required to report positions to competent authorities? Under which conditions should naked short selling be allowed? Should competent authorities be able to



take emergency measures (e.g. temporary bans on short selling or on naked short selling) within prescribed limits when they need to address specific market risks and disruptions?

Question: Is there a need to enhance risk management by financial intermediaries and banks? Should investment firms and banks be required to have necessary arrangements in place to ensure timely delivery of financial instruments traded on own account or in the context of execution of clients' orders?

CESR is currently conducting a comprehensive analysis of the short selling regimes in Member States and firmly believes that a harmonised regime for short selling across Europe is desirable. However, CESR considers this issue might be best dealt with in separate European legislation rather than an amendment to the MAD.

Other comments

According to the provisions of Art. 14(1) of MAD, it is left to the national discretion of Member States to decide on the amount of administrative pecuniary fines and the types of administrative measures applicable in market abuse cases, provided however that they are effective, proportionate and dissuasive. Furthermore, the Member States may also introduce criminal sanctions in market abuse cases.

The exercises undertaken by CESR so far have revealed that there are differences in respect of the sanctioning regimes applicable in cases of market abuse. The existing differences are partially due to the fact that Member States' legal systems differ across the EU, and that the division of responsibilities between competent authorities in each Member State, in relation to the investigation of cases and subsequent enforcement action also varies. Administrative sanctions and measures range from a public or private reprimand to monetary penalties (pecuniary fines), disqualification from management or ownership of a regulated entity, withdrawal of licenses, or require settlement of a case. There is also quite a divergence in the amounts of administrative pecuniary fines available to authorities.

The ability of securities regulators to take administrative measures or impose sanctions on those who do not comply with the relevant provisions of MAD is of high importance to allow them to effectively perform their tasks. Therefore, their capacity to act on a level playing field especially when performing enforcement and sanctioning activities is considered by CESR as a precondition to a credible EU supervisory system and fundamental to maintaining sound financial markets, on which their participants have confidence. At the same time, such equivalence in enforcement and sanctioning powers protects European financial markets from regulatory arbitrage.

In addition, it should be taken into account that market abuse, and in particular market manipulation strategies, are scale-free: the same strategy can be carried out in very small-scale (for instance in an intra-day set-up) or in a very big-scale (for instance during take-overs, IPOs or long-lasting pump & dump schemes). Accordingly, CESR believes that it is necessary that the design of the sanctions should be sufficiently flexible as to be effective, proportionate and deterrent. In this respect several EU jurisdictions exhibit interesting solutions.