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CITY OF LONDON LAW SOCIETY COMPANY LAW COMMITTEE

Revision of the Market Abuse Directive

Response of the Company Law Committee of the City of London Law Society

The City of London Law Society (CLLS) represents approximately 13,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees and in this case the response has been prepared by a working party of the CLLS Company Law Committee.

The Company Law Committee welcomes the opportunity to participate in the public consultation on the revision of the Market Abuse Directive. We will comment on only the following questions.

- Questions relating to the extension of MAD to financial instruments admitted to trading on MTFs (questions (4), (5) and (6)).

- The requirement for an issuer to notify the competent authority if it delays disclosure of inside information (there is no question relating to this proposal).

- Whether a competent authority should have responsibility for deciding that there should be a delay of disclosure of inside information where an issuer needs emergency lending assistance (question (11)).

- Whether there are other areas where it is necessary to progress towards a single rule book (question (14)).

We have not commented on the questions in relation to enforcement powers and sanctions because those are focussed on the enforcement of the prohibition of market abuse, not on the issuer's obligation to disclose information under Article 6 of MAD. The arguments that support the enhanced harmonisation of sanctions for the market abuse prohibition (which may have effects beyond the borders of a Member State) do not apply to enforcement of the issuer's disclosure obligation. We do not see any need for enhanced harmonisation of the enforcement of issuers' obligations and any steps in that direction would require significantly greater

harmonisation of the approach to implementation of those obligations, which we address in our response to the questions on the single rule book.

1. Questions relating to the extension of MAD to financial instruments admitted to trading on MTFs (questions (4), (5) and (6))

The UK's prohibition of market abuse covers financial instruments admitted to trading on MTFs. It has done so since before adoption of the Market Abuse Directive. As a result the proposed extension of the scope of MAD would not have a significant effect in the UK in relation to the prohibition of market abuse (insider dealing and market manipulation). We believe this approach makes sense and do not see any basis for differentiating MTFs from regulated markets for the purposes of preventing abusive behaviour.

However, we do not see any justification for extending the obligation to disclose inside information to issuers who only have instruments admitted to trading on a MTF. It should be a matter left to each MTF to define the scope of the disclosure obligation applicable to issuers whose securities they admit to trading. That will allow a proportional approach that will take into account differences between markets. In the UK, AIM operates disclosure standards that are tailored to the kinds of issuers whose shares are traded on its market. These standards are similar to, but in their detailed application less onerous than, the equivalent requirements of MAD. These rules operate satisfactorily in practice, relying to a large extent on the involvement of Nominated Advisers, which is a special feature of AIM. To introduce rules implementing Article 6 of MAD would increase costs for issuers without any material improvement in the quality of information disclosed to investors.

If, as we suggest, each MTF defines the scope of the obligation to disclose information, it would not be necessary to have an adapted regime for SMEs admitted to trading on MTFs. In relation to regulated markets, we think it will be confusing for investors if different disclosure regimes apply to different companies admitted to trading on the same market and we do not support an adapted regime for SMEs traded on regulated markets.

2. The requirement for an issuer to notify the competent authority if it delays disclosure of inside information (there is no question relating to this proposal)

In paragraph 2 of Section C, it is suggested that the discretion allowed to Member States whether or not to require issuers who delay the public disclosure of inside information to notify the competent authority should be withdrawn so that in all cases issuers who delay disclosure would be required to make that notification. We note that while Article 6 of MAD refers to notification of the decision (to delay disclosure) "without delay", the specific proposal (which we understand follows the approach to implementation adopted in Germany), is to require notification when the inside information is announced. No explanation is given of why this is thought desirable, or how the ex post notification enhances the ability of the competent authority to enforce the disclosure obligation.

This proposal is justified on the basis that it would represent progress towards a single rule book. However, we do not accept that as a sufficient justification for withdrawing a discretion

that is very important to the UK market. Specifically it is suggested that the benefits of the change are *"reducing the risk of any regulatory arbitrage, of increasing the effectiveness of the legislative framework and of diminishing costs for firms who have to comply with different rules in different markets"*. We do not believe that any of these justify the change proposed.

"reducing the risk of any regulatory arbitrage"

We do not believe there is any evidence that continuous disclosure obligations play an important part in decisions by issuers choosing the trading market for their securities. We do not therefore see how there can be said to be any risk of regulatory arbitrage.

"increasing the effectiveness of the legislative framework"

It is not clear how the effectiveness of the legislative framework is reduced by allowing a discretion that was initially allowed in order to reflect different regulatory approaches in different markets, those being considered the most effective in local conditions. What has changed in seven years?

"diminishing costs for firms who have to comply with different rules in different markets"

For reasons that are well understood (principally the difficulty of maintaining sufficient liquidity in several markets) there are relatively few issuers with multiple listings within the EEA. Those that have multiple listings are large enough to absorb the costs of compliance with different rules. Those costs will only be saved if there is true harmonisation (in the practical application of the rules and their enforcement) and in any event must be set against the additional costs for issuers complying with a new rule.

We believe that the principle of subsidiarity requires that it is not sufficient to assert that the proposed measure is justified by "the objective of enhancing convergence across the EU".

We think the way the MAD obligation to disclose inside information is operated within the UK would render the obligation to notify the competent authority disproportionately burdensome both for issuers and for the competent authority. The usual case for an issuer to delay disclosure of inside information relates to impending transactions where negotiations are continuing on a confidential basis. In any such case, identifying the moment in time when the progress of the negotiations has reached a stage such that inside information may be said to exist requires difficult judgments. Similarly difficult judgments are required when an event occurs (or is discovered) but it is not immediately clear what are the implications of that event or where it is not known with certainty what has occurred and an investigation is required in order to establish the facts.

Against that background, we question what value is gained by requiring the notification of the decision to delay to the competent authority after the disclosure of the inside information has taken place. If that disclosure leads to a significant movement in the price of the issuer's securities the competent authority may, if circumstances justify it, ask the issuer to explain the circumstances (this is how the FSA operates). In the case of the announcement of a transaction

that has been kept confidential typically there would be no need to investigate the decision to delay and no need therefore to undertake the assessment of the moment in time when disclosure of inside information was delayed. We understand that the governance system in Germany makes it easier to identify the time when the decision to delay is taken.

We do not believe there is any evidence within the UK regulated markets that an obligation to notify the competent authority in these circumstances would improve the overall level of compliance with the obligation to disclose inside information.

3. Whether a competent authority should be granted the power to decide the delay of disclosure of inside information where an issuer needs emergency lending assistance (question (11))

We agree that in situations where financial institutions are in a grave condition with implications for systemic risk or for a Member State's financial stability, the financial institution should be entitled to delay disclosure of inside information. We believe that is the effect of Article 6 of MAD as it currently stands. No amendment is therefore required, although Level 3 guidance may be helpful.

We do not agree that the decision to delay should be made by the regulator itself. We would expect a financial institution in the circumstances described to pay particular heed to the views of its regulator, the relevant central bank or other government authority to determine whether information about the state of the institution should be made public. However, we do not see any justification for taking that decision out of the hands of the issuer itself which will be in the best position to weigh up the interests of its shareholders and other stakeholders and those of the issuer itself.

We note that in the description of the conditions to be satisfied for the competent authority to require delay in the disclosure, there is no mention of the requirement that the omission would not be likely to mislead the public. We agree with that approach. As we suggested in our response to the Call for Evidence on the MAD review in 2009 (a copy of which is attached), we think the condition requiring that the delay not be misleading is confusing. We strongly recommend that in the review of MAD that condition should be removed. We note, and agree with, the observation in the first paragraph of Section C2 that "*Further clarification could be enhanced by clarifying the conditions for deferred disclosure*" but full consultation on the terms of that clarification would be required.

In this connection we also note that the approach to implementation of MAD in the UK treats the requirement for emergency lending assistance to support an institution differently from the circumstances that gave rise to that requirement. Any rule that provided a special right to delay the disclosure of the assistance should also be clear that disclosure of both the assistance and the requirement for it can be delayed.

4. Whether there are other areas where it is necessary to progress towards a single rule book (question (14))

As we have stated, we do not see progress towards a single market as an end in itself as sufficient justification for further harmonisation. We are not aware of any other aspects of Article 6 of MAD that require further harmonisation.

However, there are a number of aspects of MAD that in our view should be amended. These are described in our 2009 response.

6 August 2010