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# Market abuse across Europe - investigations, compliance and MAD II



# Introduction

CMS advises a wide variety of financial institutions across Europe - assisting with market abuse compliance and handling investigations and enforcement cases.

We find that firms struggle to cope with the complexity of the different national regimes that have grown up since the EU's Market Abuse Directive (MAD I). These problems make compliance difficult and pose real challenges when suspicious transactions are investigated by several authorities, often under very different national procedures, without any sensible coordination.

Financial institutions will have to deal with the new EU legislation, known as MAD II. Firms need a truly European solution and expert advice across the differing national regimes. Inspired by our experience of domestic and cross border work across Europe and to help firms meet the challenges of MAD II we have designed the CMS online market abuse resource (go direct to www.law-now.com/marketabuse) which analyses EU legislation and the domestic regimes in 19 countries.

We hope that you will find it useful.




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# Dealing with the differing national market abuse regimes

Member states have implemented MAD I on a minimum harmonisation basis with the result that member states have maintained and developed widely differing national regimes.

The main difficulties relate to the scope of the many over-lapping prohibitions and the different views that regulators take on permitted activities and accepted practices. Many member states have altered or expanded upon the MAD I provisions, some have additional legacy provisions, and most have an additional and over-lapping criminal regime. In the UK, for example, there are prohibitions implementing MAD I and there are also additional prohibitions that existed before MAD I and which are broader (and super-equivalent).

There is also a huge difference in the approach to products traded on a primary multilateral trading facility (MTF) – some countries have not extended market abuse beyond those products that are traded on regulated markets, others have extended the full regime to all MTFs, while some countries have partially applied the regime to MTFs (some applying only some of the rules and some applying the regime to only some MTFs). The position is further complicated by the fact that some member states have extended the definition of financial instruments to include the broader list in MiFID.



It is difficult for firms to establish exactly what is, and is not, prohibited. Traders and compliance teams face a bewildering web of over-lapping and conflicting regimes. One regulator may regard a given scenario as acceptable, whilst another regulator may view the same facts as market abuse.

## The areas in which national regimes differ



# The different investigatory procedures across Europe

## The danger of multiple investigations

Firms have to deal with hugely different national procedures for investigating and 'prosecuting' market abuse. The CMS online market abuse resource has flow diagrams to explain the local procedure in each country.

Firms often assume that the process will be similar to that in their home country but are often shocked when they experience the different procedures in other jurisdictions in areas such as:

- the warning required before a defendant is summoned, in France it is as little as eight days
- the process for an administrative investigation leading to a criminal case
- whether there is a process for an agreed settlement
- the timeframe for appeals, which varies from 8 to 30 days.

There is no system (such as the home/host provisions under the single passport) to ensure that there is a single investigation of a suspicious transaction (for example by a single regulator or through a coordinated process). Instead firms are plunged into a system that encourages and facilitates multiple, uncoordinated investigations by the authorities of different countries into the same transaction. Even where a firm has been cleared by one regulator there is nothing to prevent another authority from conducting their own investigation into exactly the same transaction.

This means firms face multiple regulators, all judging the evidence under their own differing regimes and all of whom have different attitudes to the prosecution of market abuse in general, and to the acceptability of various market practices.

These experiences can be costly and time consuming; it can be very alarming to find that overseas regulators are able to take such a different stance.

**Mutual assistance**

Where an authority requires evidence from a person or firm in another country, it may conduct its own investigation directly, but it also has the power under MAD I to request mutual assistance from the authorities in that other country. A trader may therefore find that he is interviewed by his home regulator but that authority may be acting effectively as an investigatory agent for a prosecuting authority in another country.

The mutual assistance provisions of the directive mean that information and evidence gathered by the firm's home regulator (for example, by information requests or in interviews) may be passed to, and used by, the authorities in other member states. These authorities may follow very different procedures in their investigation, enforcement and prosecution of market abuse; they may have more severe regimes and may have a different attitude to market practices involved. Firms therefore need to be alive to these risks and have access to advice and information about the different national regimes and the risks that they pose.

## Increasing investigation and enforcement across Europe

In future the European Securities and Markets Authority (ESMA) in Paris will have an important role; ESMA is the new EU authority which replaced CESR under the new European System for Financial Supervision. It is charged with raising enforcement standards across the EU. There is a belief that market abuse remains widespread despite the introduction of MAD I and there is a clear priority to be seen to be cracking down on insider dealing, market manipulation and late disclosure of price sensitive information.



Financial institutions have to cope with an absurdly complex process when suspicious transactions (or other suspicions of possible market abuse) are investigated. Rather than a single investigation under one process, a suspicious transaction is liable to be investigated by several regulators operating different processes, on different timescales and against different benchmarks.

In the UK, the FSA has stepped up its enforcement programme by augmenting the, already substantial, manpower of its enforcement division, and increasingly pursuing large fines and criminal convictions. Recently there have been large fines against firms and individuals (for example, £6 million against an individual for market manipulation). By the end of 2011 the FSA had secured criminal convictions against 11 individuals.

Historically some member states have done relatively little to enforce their market abuse regime under MAD I. Firms can therefore anticipate that pressure from ESMA will result in drastic increases in enforcement activity and much higher penalties.

# Coping with change - MAD II



ESMA, the new EU authority, will need to make sense of MAD II; the jury will remain out on whether it will really be able to achieve co-ordinated investigation and enforcement of a single European rulebook. We are very doubtful that this will be achieved.

Firms must now prepare for the reform of market abuse regulation under the 'MAD II' legislation. This seeks to address issues identified in the European Commission's review of MAD I and was launched in parallel with the revisions of MiFID under MiFID II. The new EU legislation takes the form of a new Market Abuse Regulation (MAR) which will have direct effect (without requiring domestic implementation) and a new directive introducing EU requirements for criminal sanctions (under the Lisbon Treaty). Firms will need to prepare for the changes to be introduced under MAR; these are analysed in detail in the CMS online market abuse resource.

The changes include:

— the extension of the EU regime, for example, to protect junior trading venues that do not qualify 'as regulated markets'
— broadening the prohibitions
— strengthening investigatory powers and sanctions.

It will be hard for firms to assess the impact of the new legislation because the present national market abuse regimes vary hugely from country to country, so the 'gap' analysis will vary too.



Extending MAD I to primary MTFs seems logical to regulators, but the requirements and prohibitions were not designed for these markets or for the instruments traded upon them. There are real concerns about the end result for this diverse group of trading venues and the different products traded.




# How CMS can help - a European solution to a European problem

Our experience working with financial institutions has highlighted the need for a truly European solution.

With 5,000 people working in 48 cities across 30 countries, CMS has the most extensive European footprint of any law firm. It is therefore ideally placed to deal with the pan-European challenges of market abuse regulation and enforcement.

Our people are immersed in the local culture and understand the legal and regulatory landscape. It means our clients benefit from high quality expertise wherever they need it in Europe, delivered in the local context. Working closely together, our market abuse team has prepared this online market abuse resource.

It is an invaluable resource for CMS clients and it underpins the 'paid for' services we provide, such as:

— advisory work such as assurance and systems review
— helping with investigations and enforcement
— market abuse training.

## The CMS pan-European online market abuse resource

We have developed the CMS online market abuse resource to assist fund managers and other financial institutions. It draws on extensive research from expert, dedicated teams across our European offices. Our core market abuse team covers 15 EEA states, as well as other countries such as Switzerland.

The resource provides extensive material to aid market abuse compliance with a variety of 'tools' including:

— materials on the evolving MAD II regime including MAR
— analysis on the impact of MAR
— a tracker feature giving the latest news on the progress of the MAD II reforms
— a database of regulated markets across the EEA
— a database of MTFs operating across the EEA, identifying those home countries which have applied the market abuse directive prohibitions
— country by country flowcharts and detailed descriptions of the different national investigatory and enforcement procedures
— a database of the competent administrative and criminal authorities in each country and the various national-level guidance they have issued
— a database of the national rules and legislation implementing the market abuse directive and where they can be found
— a database of the national requirements on the submissions of suspicious transaction reports.

If you have any questions about market abuse legislation, the assistance CMS can provide or if you would like to view the CMS online market abuse resource please:

— email or telephone the contact for your country (contact details are provided on the enclosed contact sheet) or
— go direct to www.law-now.com/marketabuse.

## Market Abuse Investigations - how CMS can help

We are familiar with the pitfalls which financial institutions face when 'suspicious transactions', and other activities, are investigated as potential market abuse. We handle investigations; these may be domestic enquires or those that involve a number of different authorities in more than one country. Some of these involve the mutual assistance procedure.

In our online service, detailed flowcharts show the different procedures and provide an immediate help to firms faced with an investigation and a valuable start point for bespoke advice from the CMS team.

We help institutions familiarise themselves with the different procedures and assist and represent them during the investigatory and potential enforcement process. This includes investigation of individuals, firms and their senior management for failure in their internal compliance processes. We can assist with all aspects – reviewing evidence and advising on the position under the different national prohibitions, assisting in responding to documentary requests and handling interviews. We also prepare formal representations and handle any cases that proceed further to the enforcement stage.

## Pan-European Advisory Services - Assurance and Systems Review

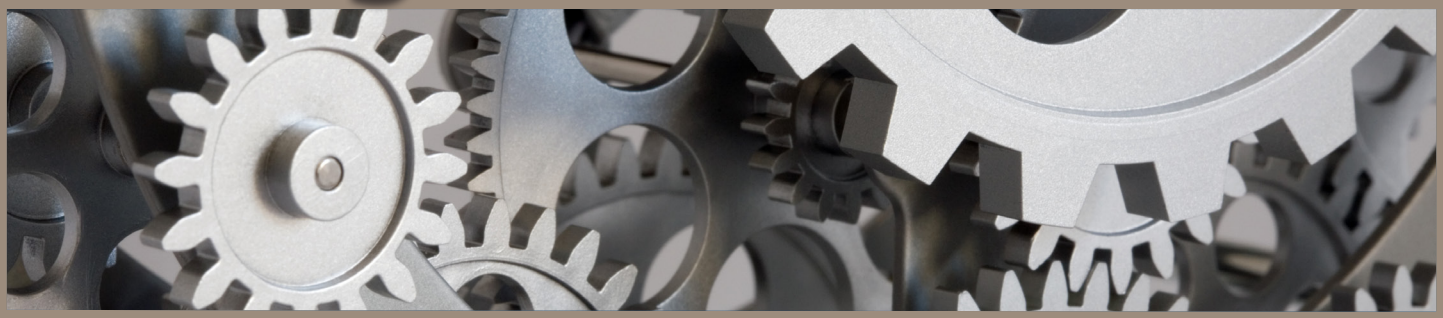
We help financial institutions to develop and benchmark their internal compliance procedures, taking account of the differing national regimes. We assist firms to assess and mitigate the risk of market abuse breaches.

We provide advice to legal and compliance departments on individual scenarios and transactions that raise market abuse issues. We handle the complex issues that arise in determining the precise scope of the national regimes and what is and is not accepted by the different authorities. We also assist in dealing with the regulatory obligations concerning suspicious transaction reporting, research departments and Chinese wall procedures.

## Market abuse training

CMS provides training to financial institutions as part of the firm's market abuse compliance. We use our internal resources to develop a bespoke training program that we deliver on site. We often provide multiple sessions, for example, when training an entire trading floor.


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RegZone
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**The Regulatory Zone (RegZone)**

A 'free to view' online resource for CMS clients and contacts, providing a wealth of materials to help financial institutions deal with the fast-changing world of regulation.

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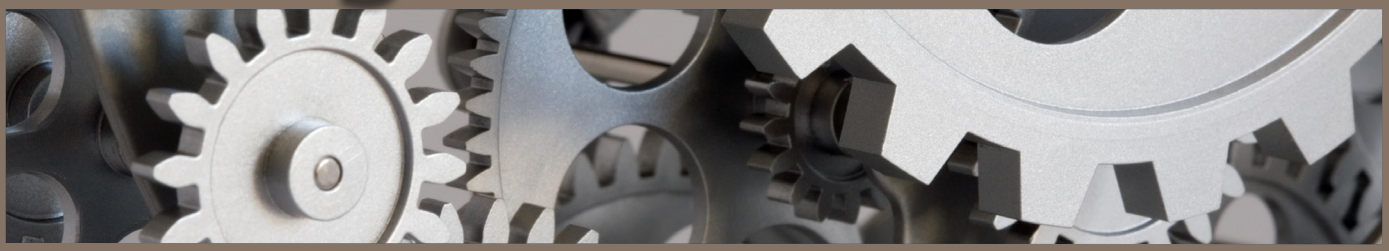
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