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EU Market Abuse Regulation and asset managers – guidelines for persons receiving market soundings

On 28 January 2016, the European Securities and Markets Authority ("ESMA") published a consultation paper containing draft guidelines on the EU Market Abuse Regulation ("EU MAR"). The consultation paper contains proposed guidelines for persons receiving market soundings (the "**Guidelines**"). Although the consultation is open until 31 March 2016 and the Guidelines are still in draft form, firms should nonetheless use them now as the basis for their preparations for implementing EU MAR. This is because the final version of the Guidelines may not be published before 3 July 2016 - the date that the majority of the provisions in EU MAR will take effect. The consultation paper is available [here](#).

The FCA has also indicated that it may provide further guidance on the market soundings regime in the first half of 2016, but if any such guidance is issued, it is likely to supplement ESMA's work in this area.

We set out below:

- an overview of the market soundings regime;
- a summary of the requirements applicable to the persons communicating the information (disclosing market participants, or "**DMPs**");
- a summary of the Guidelines for market sounding recipients ("**MSRs**"); and
- a further explanation of certain aspects of the Guidelines relating to the MSR's assessment of whether information is inside information.

A: OVERVIEW OF THE MARKET SOUNDINGS REGIME

In summary, under EU MAR a market sounding comprises:

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- the communication of information, prior to the announcement of a primary or secondary offer, by the issuer or secondary offeror (or a third party acting on its behalf), in order to gauge the interest of potential investors in a possible transaction and the conditions relating to it, such as its potential size or pricing; or
- the communication of information in certain circumstances by a person intending to make a take-over bid or undertake a merger.

A market sounding as defined may or may not involve the communication of inside information.

Information communicated in other circumstances and/or by a person in a capacity other than those listed above will not amount to a market sounding as defined, but again may or may not involve the communication of inside information. While the market sounding regime is limited to particular scenarios, it is possible that regulators will expect some similar safeguards to be in place in other circumstances where inside information is, or may be, disclosed.

B: THE MARKET SOUNDINGS REGIME FOR DMPs

The scope of the market soundings regime in EU MAR is important, because those provisions provide a specific "defence" to DMPs in relation to the prohibition on the unlawful disclosure of inside information, provided that a number of highly detailed requirements are satisfied. These requirements are set out in detailed technical standards drafted by ESMA (the "**Technical Standards**") and include:

- a standard set of information that must be included in communications to MSR, informing the MSR of whether or not the information being provided amounts to inside information, estimating when any inside information that is to be communicated will cease to be inside information, and seeking consent to proceeding with the relevant sounding;
- recording data in relation to natural persons within MSR who receive information during the course of a sounding;
- notifying MSR when any inside information communicated during a sounding ceases to be inside information; and
- detailed record keeping requirements, including the requirement to maintain written minutes or notes of any soundings taking place via unrecorded meetings or telephone conversations and to agree such minutes with the relevant MSR, or otherwise to keep a copy of the MSR's written minutes of the sounding with the DMP's own minutes.

If a DMP does not comply with the Technical Standards, or does not fall within the scope of the market soundings regime, the specific market soundings defence in relation to an allegation of unlawful disclosure of inside information under EU MAR will not be available, although it may still be possible (albeit potentially more difficult) if certain conditions are met to argue that such a disclosure occurs in the normal exercise of the DMP's employment, profession or duties and is not therefore unlawful. Careful consideration would need to be given to safeguards that would need to be applied in such a situation and it may still be relevant to consider the general substance and overall objectives of ESMA's Technical Standards. At a minimum, necessary safeguards are likely to include the imposition of a confidentiality undertaking and the maintenance of a record of the disclosure and the reasons for it.

C: GUIDELINES FOR MSR - SUMMARY OF KEY POINTS

The following list sets out key points contained within the Guidelines. It is important to note that these requirements will apply to all MSR, whether they are regulated firms or not.

- **Contacts for market soundings:** MSR may choose to designate a particular person or contact point within their organisations to receive market soundings, although importantly, this is not mandatory. If MSR do choose to have such a contact, they should ensure that the relevant contact information is made

available to DMPs - for example, directly or through intermediaries or via a website. The Guidelines also state that it would be good practice for the MSR to keep evidence of the designation of the relevant contact.

- **Notification of desire not to receive market soundings:** After being contacted by a DMP, an MSR should notify the DMP whether or not the MSR wishes to receive future market soundings and, if so, whether in relation to all potential transactions or only particular types of potential transactions. In practice, some firms may prefer to make this known in the same way as they make known their contacts for market soundings (if any), rather than awaiting the first contact from a DMP.
- **MSRs to assess whether information communicated during the sounding is inside information:** EU MAR requires MSRs to perform their own independent assessments of whether the information that they receive from a DMP during a sounding is inside information and when it ceases to be inside information. The Guidelines expand on these requirements - see [Part D](#) below.
- **Written minutes or notes of unrecorded meetings or conversations in relation to a market sounding:** Where a market sounding is not recorded (for instance, where it is made at a face-to-face meeting), the Technical Standards would require the DMP to maintain a written record of the relevant discussion which, if agreed, must be signed by the DMP and the MSR. Where the MSR disagrees with the DMP's record, the DMP's record must be kept with the MSR's signed alternative version of the meeting or conversation. The Guidelines mirror the requirements in the Technical Standards by requiring MSRs to either sign the DMP's minutes if they agree with their content, or otherwise provide the DMP with a signed version of the MSR's own set of minutes within five working days of the sounding if they do not agree with the DMP's record of events.
- **Internal procedures to control the flow of information received during a market sounding:** MSRs will be required to establish, implement and maintain internal procedures to manage the flow of any information received in the course of a market sounding within the firm, and to ensure that such information is communicated only through particular specified internal reporting lines on a "need-to-know" basis. For firms that only maintain an external perimeter and do not currently restrict access to information within the firm, this will require new policies and procedures to ensure that information obtained during a sounding is only available to those individuals who have a justifiable interest in accessing it. This may pose a particular difficulty in smaller firms and/or in firms whose internal structure does not easily accommodate separate lines of communication.
- **Insider lists:** For each market sounding, MSRs must draw up a list of persons working for them who are in possession of information communicated during the course of the sounding. Although ESMA has published a separate set of technical standards relating to the required format of insider lists that apply to issuers and firms acting on behalf of, or for the account of, issuers, these do not apply to MSRs. MSRs therefore have more flexibility about the precise format in which to compile and maintain insider lists in connection with market soundings, but the Guidelines indicate that a separate list should be maintained for each separate sounding. Where multiple soundings take place in connection with a particular transaction, this will therefore necessitate separate lists being maintained in relation to the information provided under each sounding. As a result, these requirements may be onerous in nature.
- **Internal training:** MSRs will need to ensure that the function or body within the firm that is responsible for assessing whether inside information has been received as a result of a market sounding is composed of staff that have been properly trained for that purpose. In addition, staff who receive or process information in the course of a market sounding must receive proper training on the MSR's internal procedures and on the prohibitions under EU MAR relating to insider dealing and improper disclosure of inside information.
- **Identification of related issuers and financial instruments:** Where the MSR considers that it has received inside information during a market sounding, the MSR must identify all issuers and financial instruments to which that inside information relates. In its explanatory text, ESMA says that this exercise should extend to the identification of "related financial instruments". This may be an onerous obligation to the extent that it could require the identification of a wide range of instruments which may be connected

with securities of the issuer to whom the inside information relates. Not all related financial instruments will be capable of identification.

- **Record keeping:** MSRs must maintain records in a durable medium of each of the following for at least five years:
 - any notification to a DMP relating to whether the MSR wishes to receive market soundings;
 - any assessment carried out by the MSR as to whether information received during the course of a market sounding is inside information (including the reasoning supporting that assessment);
 - any differences in opinion between the DMP and the MSR as to whether information communicated during a market sounding is inside information;
 - the MSR's internal procedures relating to the control of the flow of inside information and to training;
 - any insider lists drawn up in connection with a market sounding; and
 - any assessment of related instruments and issuers following receipt of inside information during a market sounding.

While some of the Guidelines may address matters which MSRs may already do as a matter of good practice (including steps which the FCA identified as good practice in its thematic review in 2015 ([TR 15/1](#))), compliance with others is likely to require the introduction of stringent procedures and the maintenance of detailed records.

D: MSR'S ASSESSMENT OF INFORMATION RECEIVED DURING A MARKET SOUNDING

- The MSR's assessment of whether information that has been received during a market sounding constitutes inside information must be carried out independently from the DMP's analysis of that information – i.e. the MSR should not simply adopt the DMP's opinion of the status of the information. The MSR must take into account all information available to it, which may include information that is not available to the DMP.
- In some circumstances, the MSR is required to notify the DMP that it has reached a different conclusion from the DMP about the status of the information, but this depends upon the basis for the MSR's analysis:
 - if the DMP has originally concluded that the information provided during the course of the market sounding was not inside information and the MSR, after performing its own analysis, disagrees with that assessment, the MSR must inform the DMP of the reasons for the difference in opinion if the assessment is based exclusively upon the information received from the DMP;
 - however, if the difference in opinion is based in part or in whole upon other information that is available to the MSR, but which was not communicated by the DMP as part of the market sounding, the MSR must not inform the DMP that it has reached a different conclusion. This is to ensure that the MSR does not disclose any other information within its possession which may itself amount to inside information.
- Where the DMP informs the MSR that the information provided during the course of a sounding is inside information and the MSR, after carrying out its own analysis, concludes that the information is not in fact inside information, the Guidelines do not impose an obligation on the MSR to inform the DMP of this fact.
- In such a situation, the MSR may choose to use the relevant information as it wishes, but the MSR will be liable if it subsequently transpires that the information is inside information and the MSR's actions have contravened one or more provisions in EU MAR. Given the significant risks in such a scenario, MSRs would need to be certain of the accuracy of their analysis before disclosing, or trading on the basis of, such information.

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- The DMP must notify the MSR that information provided under a market sounding no longer constitutes inside information. A similar approach to that outlined above applies in relation to such notifications - i.e. the MSR must carry out its own independent assessment to satisfy itself that the information has in fact ceased to be inside information. If the MSR disagrees with the DMP, it must inform the DMP of the reasons for the difference in opinion, unless that difference is based on information other than which was received from the DMP under the market sounding.

FOR FURTHER INFORMATION, PLEASE CONTACT

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