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The Reform of the EU Market Abuse Law: Revolution or Evolution?

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Abstract: This paper discusses whether the forthcoming reform of market abuse law, as proposed by the EU Commission in October 2011, may be seen as a 'revolution' or a mere 'evolution'. Section 1 explains the topicality of regulating market abuse (ie insider dealing and market manipulation), both in the US and the EU. Section 2 analyses to what extent the transformation of the current Market Abuse Directive into a Regulation and the new Directive on criminal sanctions may be regarded as 'revolutionary'. Section 3 deals with the substantive changes which seem to be more 'evolutionary' in updating and improving some aspects of the previous law. In section 4 we briefly discuss our main concerns with the proposed reform.

Keywords: market abuse, insider dealing, market manipulation, Market Abuse Directive, securities regulation

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1. Introduction

This article discusses the forthcoming reform of market abuse law as proposed by the EU Commission in October 2011. Market abuse law covers insider dealing, market manipulation and ad hoc disclosure of inside information. The reform reflects a number of recent events and discussions on both sides of the Atlantic.[1]

In the United States, for instance, the conviction and sentencing of the hedge fund manager Raj Rajaratnam to 11 years in prison for insider dealing, and the payment of US $25 million by Moore Capital Management to settle charges of market manipulation have received considerable attention. As regards legislative developments in this field, the Dodd-Frank Act of 2010 has facilitated the enforcement of market manipulation in derivative markets.[2] In addition, there have been frequent suggestions to enact a special law that would prohibit federal employees and members of Congress from trading securities based on information obtained on the job.[3]

In Europe, a number of cases have recently reached the European Court of Justice (ECJ), now the Court of Justice of the European Union (CJEU). In *Spector Photo Group NV*, a company repurchased its own shares and subsequently published new and positive results concerning its commercial policy. This provided the ECJ with the opportunity to give guidance as to the requirements of insider dealing.[4] In *IMC Securities* the CJEU clarified an aspect of the prohibition of market manipulation. In response to ambiguities of EU law, it was held that trade-based market manipulation does not require that the price of the securities be kept at an abnormal or artificial level for a certain duration.[5] Currently, another case which deals with the obligation to disclose inside information is pending at the CJEU.[6]

The foregoing cases concern the Market Abuse Directive 2003/6/EC, frequently referred to as MAD.[7] MAD is implemented by all Member States in national legislation.

[1] See Commission Staff Working Paper Impact Assessment, COM (2011) 651 final, p. 190-2 (referring to US law).
[2] Dodd–Frank Wall Street Reform and Consumer Protection Act, Pub.L. 111-203, H.R. 4173, in particular section 753.
[3] Proposals for Stop Trading on Congressional Knowledge (STOCK) Act, S 1903 (Nov. 17, 2011), S 1871 (Nov. 15, 2011), H.R. 1148 (Mar. 17, 2011); H.R. 682 (Jan. 26, 2009); H.R. 2341 (May 16, 2007); H.R. 5015 (Mar. 28, 2006).
[4] Case C-45/08 *Spector Photo Group NV, Chris van Raemdonck v. Banking, Finance and Insurance Commission (CBFA)* [2009] ECR I-12073. See also L. Klöhn, 'The European Insider Trading Regulation after the ECJ's Spector Photo Group-Decision', 7 *European Company and Financial Law Review* 2 (2010), p. 347-366; K. Langenbucher, 'The 'Use or Possession' Debate Revisited – Spector Photo Group and Insider Trading in Europe', 5 *Capital Markets Law Journal* 4 (2010), p. 452-470.
[5] Case C-445/09 *IMC Securities BV v. the Netherlands Authority for the Financial Markets*, Judgment of 7 July 2011, not yet reported.
[6] Reference for a preliminary ruling from the Bundesgerichtshof (Germany) lodged on 14 January 2011 – *Markus Geltl v. Daimler AG*, Case C-19/11.
[7] Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market abuse), [2003] OJ L 96/16. See also M. Siems, 'The EU Market Abuse Directive: A Case-Based Analysis', 2 *Law and Financial Markets Review* (2008), p. 39-49.

In addition, following the recommendations of the Lamfalussy report,[8] the current EU market abuse law is composed of a number of second-level directives and regulations which specify more technical details.[9] National regulators and courts are bound by these. At the third level, the European Securities and Markets Authority (ESMA, formerly CESR)[10] publishes guidance on the common operation of the Directive,[11] and at level four, the Commission ensures compliance with the European law.

The proposed reform of the EU market abuse law consists of two elements. On the one hand, a proposal for a Regulation on market abuse is to replace MAD, with some modifications and extensions.[12] On the other hand, the Commission has proposed a new directive specifically dealing with criminal sanctions for insider dealing and market manipulation.[13] The next steps are that these proposals will be discussed by the European Parliament, then possible amendments would be re-examined by the Commission and eventually they would have to be approved by the Council.[14] In addition, the European institutions will need to revise the current second level instruments.

The following discusses the proposed new market abuse law at two levels. Section 2 is an analysis to what extent the transformation of MAD into a Regulation and the new Directive on criminal sanctions may be regarded as 'revolutionary'. Section 3 deals with the substantive changes which seem to be more 'evolutionary' in updating and improving some aspects of the previous law. In section 4 we briefly discuss our main concerns with the proposed reform.

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[8] Final Report of the Committee of Wise Men on the Regulation of the European Securities Markets, 15 Feb 2001. See also M. Siems, 'The Foundations of Securities Law', 20 *European Business Law Review* (2009), p. 141-171 at p. 165-168.

[9] Commission Directive 2003/124/EC of 22 December 2003 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards the definition and public disclosure of inside information and the definition of market manipulation, [2003] OJ L 339/70; Commission Directive 2003/125/EC of 22 December 2003 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards the fair presentation of investment recommendations and the disclosure of conflicts of interest, [2003] OJ L 339/73; Directive 2004/72/EC of 29 April 2004 implementing Directive 2003/6/EC of the European Parliament and of the Council as regards accepted market practices, [2004] OJ L 162/70; Commission Regulation (EC) No 2273/2003 on Market Abuse, [2003] OJ L 336/33.

[10] See also N. Moloney, 'The European Securities and Markets Authority and Institutional Design for the EU Financial Market – A Tale of Two Competences: Part (1) Rule-Making', 12 *European Business Organization Law Review* (2011), p. 41-86; N. Moloney, 'Reform or Revolution? The Financial Crisis, EU Financial Markets Law, and The European Securities and Markets Authority', 60 *International and Comparative Law Quarterly* (2011), p. 521-533.

[11] See http://www.esma.europa.eu/documents/overview/10 (last visited 9 February 2012).

[12] Proposal for a Regulation of the European Parliament and of the Council on insider dealing and market manipulation (market abuse), COM (2011) 651 final of 20 October 2011 (in the following: 'Draft Regulation').

[13] Proposal for a Directive of the European Parliament and of the Council on criminal sanctions for insider dealing and market manipulation (market abuse), COM (2011) 654 final of 20 October 2011 (in the following: 'Draft Directive').

[14] See http://www.fsa.gov.uk/pages/About/What/International/pdf/MAD%20(PL).pdf (last visited 9 February 2012).

2. Framework reform: revolution?

The transformation of MAD into a Regulation means the new law will be directly applicable in all Member States. The Draft Regulation is also more detailed than MAD since some rules of the current second-level directives will be incorporated into the new text, for example, the 'preciseness' in the definition of inside information[15] and the indicators for behaviour relating to market manipulation.[16] Thus, the proposals may establish a significant change in that European harmonization of market abuse law will become deeper.

However, one can also question such an assessment. Key concepts of market abuse, such as 'price-sensitivity', 'misleading', 'artificial', 'abnormal', and so on, will still be undefined.[17] Thus, unless the ESMA or the CJEU draw clear lines, this will leave room for interpretation at the national level. There are also further reasons why one may expect divergence at the level of the Member States. Capital markets across Europe are still in quite different stages of development, as are levels of expertise among regulators and courts. Moreover, it has been found that administrative and criminal sanctions for violations of market abuse are fairly diverse across Member States.[18]

Here, however, we have to consider the new rules of the Draft Regulation and Directive. MAD, as other EU Directives, only requires that administrative sanctions be 'effective, proportionate and dissuasive'.[19] The Draft Regulation follows the same starting point,[20] but then, first, it requires that legislators provide maximum fines which are not too lenient. For instance, for legal persons the maximum administrative monetary sanctions should be at least 10 % of the company's total annual turnover in the preceding business year.[21] Second, the competent authorities are given some guidance in the application of these sanctions, for instance, requiring them to take into account the gravity of the breach and the financial position of the person responsible.[22]

With respect to criminal sanctions, the EU could not address them in the Draft Regulation since approximation of criminal laws is only permissible by way of directives.[23] In this respect, the Draft Directive requires Member States to treat intentional insider dealing and market manipulation as criminal offences.[24] As to the precise criminal sanctions it is only stipulated that these sanctions shall be effective, proportionate and dissua-

[15] Directive 2003/124, EC, Article 1(1) which corresponds to Draft Regulation, Article 6(2).
[16] Ibid., Articles 4 and 5 which correspond to Draft Regulation, Annex I.
[17] Draft Regulation, Articles 6(1)(a) and 8(1)(a).
[18] See Report on Administrative Measures and Sanctions as well the Criminal Sanctions Available in Member States under the Market Abuse Directive (MAD), CESR/07-693 and CESR/08-099.
[19] MAD, Article 14. See also M. Gelter and M. Siems, 'Judicial Federalism in the ECJ's Berlusconi Case: Towards More Credible Corporate Governance and Financial Reporting?', 46 *Harvard International Law Journal* (2005), p. 487-506.
[20] Draft Regulation, Article 24(1).
[21] Ibid., Article 26(1)(m).
[22] Ibid. Article 27.
[23] Compare the Treaty on the Functioning of the European Union (Consolidated Version), [2008] OJ C 115/47, Article 83(2) with Article 114 (the basis for the Draft Regulation).
[24] Draft Directive, Articles 3 and 4. This also includes attempted insider dealing and market manipulation.

sive,[25] though it may be suggested that the corresponding guidance of the Regulation may assist in the interpretation of these terms.

Overall, it can be seen that the proposals are keen on providing more effective and uniform enforcement of market abuse.[26] Specifically, it may also be regarded as significant that, for the first time, the EU will require some harmonization of the criminal law on market abuse and that it will specify some details on administrative sanctions that Member States have to provide. Yet, it is an open question whether in practice these changes will really be 'revolutionary' because regulators, national prosecutors and courts still seem to have substantial discretion. Thus, for the time after the adoption of the new laws, the crucial question will be whether the European institutions (Commission, ESMA and CJEU) will elaborate on these requirements, or whether these will mainly be left to the Member States.

3. Substantive changes: evolution?

Besides the general reform of the market abuse framework, there are also some more substantive changes to point out. These can be grouped into three broad categories: (i) modifications to prohibitions and obligations; (ii) adjustment of the scope of the market abuse regime; and (iii) expansion of supervisory and enforcement powers. The main developments in each of these categories will be discussed. This article does not, however, allow for an exhaustive analysis. The focus will be on the most significant changes.

Modifications to the prohibitions and obligations

The prohibition on insider trading currently contains three key elements which need to be proven before a person can be held liable. The information should be 'precise', it should (hypothetically) have a 'significant' effect on the price if it were made public, and the person should actually 'use' the information.[27] The Commission has expressed its doubts about the effectiveness of this definition. According to the Commission, certain information, for instance, information on the state of contract negotiations can be abused before an issuer is under the obligation to disclose it.[28] For this reason, it is proposed to qualify more information as inside information than under the current regime.

The Draft Regulation prohibits trades if a person has non-public information which a reasonable investor would consider 'relevant when deciding the terms on which transactions (…) should be effected'[29]. This means a significant expansion of the scope of the prohibition on insider trading. The Commission seems to have yielded to the temptation of a more instrumental approach against insider trading.[30] The proposed modification

[25] Ibid., Article 6.

[26] See also Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Reinforcing sanctioning regimes in the financial sector, COM (2010) 716 of 8 December 2010.

[27] MAD, Article 1(1).

[28] Draft Regulation, p. 9 and Recital 14.

[29] Ibid., Article 6(1)(e).

[30] This proposal has also received criticism at the public hearing on the review of the Market Abuse Directive, organized by the Committee on Economic and Monetary Affairs on 24 January 2012 (see for the

will also have an impact on the scope of the prohibition on tipping[31] and therefore on the amount of information that may be passed on to third parties or the type of investment recommendations one may make.

Trade-based market manipulation is a type of behaviour that is by nature delicate and difficult to prove.[32] It is easy to determine that a person has executed one or more transactions, but it becomes difficult if subsequently it must be determined that these transactions have caused a price impact and have secured the price at an artificial level. For this reason, it has regularly been seen that legislators explicitly aspire to loosen the prohibition (for example, by not including a *mens rea* element).[33] Notwithstanding such legislative efforts to lower the burden of proof, trade-based market manipulation remains a difficult offence to prove. Therefore, regulators and public prosecutors sometimes charge a person also with attempted manipulation should they fail to prove perfected manipulation. It is not uncommon that a whole manipulation case largely hinges on the definition of attempted manipulation.[34] This underlines the importance of an adequate definition of 'attempt'.

Yet, the Commission has provided a poor definition. The Draft Regulation prohibits 'attempting to enter into a transaction'[35] as well as 'trying to place an order to trade'.[36] Thus, this proposal would basically criminalize almost any trader. This cannot stand up to scrutiny.[37] But how could attempted manipulation be more adequately defined? It seems that most regulators wish to act if it cannot be proven (or can hardly be proven) if a person has caused an artificial price, while it can be proven that a person (i) has had an intention to manipulate, (ii) has executed transactions (or entered orders) and (iii) has had an impact on the price. Accordingly, the definition of attempted manipulation should at least include a *mens rea* element (intent to manipulate).[38] In addition, EU leg-

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contributions of the speakers http://www.europarl.europa.eu/committees/en/ECON/events.html (last visited 9 February 2012)).

[31] Draft Regulation, Article 7(3) and (4).

[32] See M. Nelemans, 'Redefining Trade-Based Market Manipulation', 42 *Valparaiso University Law Review* (2008), p. 1169-1180 at p. 1171-1176; E. Avgouleas, *The Mechanics and Regulation of Market Abuse* (Oxford University Press, Oxford 2005), p. 132-143.

[33] See Proposal for a Directive of the European Parliament and of the Council on insider dealing and market manipulation (market abuse), COM (2001) 281 final, p. 7; Ministry of Economic Development, *Reform of Securities Trading Law: Market Manipulation Cabinet Paper*, July 2003, p. 15. V. Goldwasser, *Stock Market Manipulation and Short Selling* (CCH Australia Ltd, North Ryde, 1999), p. 119, 137-138.

[34] See, for example, the Parnon Energy, Arcadia and Amaranth Advisors cases brought by the US Commodities Futures Trading Commission.

[35] Draft Regulation, Article 8(2)(a).

[36] Ibid., Article 8(2)(b).

[37] It seems that the Commission has taken the definition of perfected manipulation and has deleted the element referring to the (possible) consequences of the trades, *i.e.* an artificial price or misleading signals. The problem is that the definition of perfected manipulation does not contain a *mens rea* element to fall back on. The result is a definition of attempted manipulation that basically covers any trader.

[38] This does not necessarily mean that a *mens rea* element should also become part of the prohibition on perfected manipulation. Since perfected manipulation requires proof of an artificial price or misleading signals, regulators will in practice often be forced to prove (or at least to provide arguments) that a person executed the trades with an intent (or at least with an aim) to manipulate. Proof that a person is responsible for an artificial price or misleading signals without any arguments that there was an aim to manipulate the market is rather difficult to establish. However, if EU legislators were to decide to include a *mens rea*

islators should consider restricting the attempt to situations in which a person has actually executed transactions (or entered orders) and has had an impact on the price.

Due to the widespread increase in the use of automated trading methods, the Commission considered it opportune to provide specific examples of trade-based market manipulation using algorithmic trading and high frequency trading. Those examples are only meant to clarify such behavior since the strategies already fall within the current prohibition against market manipulation. Examples that are given are 'stuffing, layering, spoofing and trading for the purpose of disrupting a trading system or making it more difficult to identify genuine orders on a trading system'.[39]

Under MAD, issuers have an obligation to disclose inside information without delay. The disclosure obligation relies on the same definition of inside information as the prohibition on insider trading. In practice this often leads to situations in which certain information is in fact too premature for the issuer to disclose, while, at the same time, insiders could possibly misuse the information by trading on it. Hansen and Moalem have eloquently explained this twofold notion of inside information.[40] Therefore, to resolve this inherent tension, it was suggested by the European Securities Markets Experts Group (ESME) to introduce two separate definitions of inside information, one for the disclosure obligation and one for the prohibition on insider trading.[41]

The suggestion to introduce distinct definitions of inside information has been discussed by the Commission but was never openly supported in the preparatory documents.[42] Thus, it is remarkable that the Commission has, effectively, proposed to introduce distinct definitions. The language of the disclosure obligation in the Draft Regulation is similar to the language of the disclosure obligation under MAD. However, the prohibition on insider trading under the Draft Regulation has a lower threshold since it is also applicable to information which a reasonable investor considers 'relevant when deciding the terms on which transactions (…) should be effected'[43].[44]

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element in the definition of attempted manipulation, it seems reasonable to also include such an element in the definition of perfected manipulation.

[39] Draft Regulation, Article 8(3)(c) and p. 8. The proposal for a revised MiFID contains additional measures against algorithmic trading and high frequency trading. See Proposal for a Directive of the European Parliament and of the Council on markets in financial instruments repealing Directive 2004/39/EC of the European Parliament and of the Council, COM (2011) 656 final of 20 October 2011.

[40] J.L. Hansen and D. Moalem, 'The MAD disclosure regime and the twofold notion of inside information: the available solution', 4 *Capital Markets Law Journal* (2009), p. 323-340.

[41] ESME Report, Market abuse EU legal framework and its implementation by Member States: a first evaluation, July 6th, 2007, p. 5-9. See also C. Di Noia and M. Gargantini, 'The Market Abuse Directive disclosure regime in practice: some margins for future actions', 54 *Rivista delle società* (2009), p. 782-835.

[42] EU Commission, Call for evidence on the review of the Market Abuse Directive, 20 April 2011, p. 9-11. The Commission does not make any substantial reference to the definition of inside information in the subsequent documents: EU Commission, Public consultation on a revision of the Market Abuse Directive, 25 June 2010, p. 13-14 and Commission staff working paper, Impact assessment accompanying the Draft Regulation and the Draft Directive, SEC (2011) 1217 final of 20 October 2011.

[43] Draft Regulation, Article 6(1)(e).

[44] See also C. Di Noia, Public Hearing on the review of the Market Abuse Directive, Committee on Economic and Monetary Affairs, 24 January 2012, p. 2-3.

Given that the Commission has proposed to introduce distinct definitions, in practice this could possibly result in a more lenient disclosure regime for issuers, even though the language of the disclosure obligation is unchanged. The reason is that regulators and judges do not have to be as wary anymore that their interpretation of the disclosure obligation will also have an impact on the scope of the prohibition on insider dealing. It should be noted, however, that the actual meaning of this proposal may be influenced by the anticipated preliminary ruling of the CJEU in *Daimler*.[45]

A further point of interest is how issuers should deal with information of systematic importance, for example information on preparations of a bailout of a bank. Premature disclosure of such information could harm the public interest. The Commission has proposed that regulators, upon a request by the issuer, may permit a delay of disclosing information of systematic importance.[46]

Finally, it is interesting to note that the disclosure regime provides more lenient requirements for SME growth markets. The disclosure of inside information may be carried out in a simplified way. This is to limit compliance costs and disincentives. Also, small and medium sized enterprises (SMEs) may benefit from more lenient obligations to keep insiders' lists and to report managers' transactions.[47]

Adjustment of the scope of the market abuse regime

MAD's primary concern is to protect 'regulated markets' against market abuse. MAD applies to any financial instrument admitted to trading on a regulated market irrespective of whether or not the transaction itself takes place on that market.[48] Yet, the Draft Regulation has an extended scope.

First, the Commission wishes to protect investors against market abuse, in principle irrespective of the type of market. Given that multilateral trading facilities (MTFs) and other new types of organized trading facilities (OTFs) have gained sizeable market shares over the last decade, the Draft Regulation not only applies to financial instruments that are admitted to trading on regulated markets but also to financial instruments that are traded on MTFs and OTFs.[49]

Secondly, alternative ways of benefiting from inside information were insufficiently covered by MAD, according to the Commission. For this reason, the Draft Regulation now also prohibits insider trading with respect to instruments (such as contracts for difference) whose value is dependent on financial instruments admitted to trading on regulated markets or traded on MTFs and OTFs.[50]

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[45] See Section 1., above.
[46] Draft Regulation, Article 12(5).
[47] Ibid., Article 12(7), 13(2) and 14(2).
[48] MAD, Article 9.
[49] Draft Regulation, Article 2(1)(b).
[50] Ibid., Article 2(2).

Thirdly, it follows from the explanatory memorandum that the Commission is apprehensive of cross-market manipulation. Accordingly, the Draft Regulation also covers (i) trading in instruments, such as over-the-counter (OTC) derivatives, which could have an impact on the price of financial instruments admitted to trading on regulated markets or traded on MTFs and OTFs, (ii) trading in spot commodity contracts which could have an impact on the price of such a financial instrument and (iii) trading in instruments, such as OTC derivatives, which could have an impact on the price of spot commodity contracts.[51]

Fourthly, the market abuse regime is proposed to apply to emission allowances. This is the result of the reclassification of emission allowances as ‘financial instrument’ as part of the review of the Markets in Financial Instruments Directive.[52]

Given the foregoing, the Draft Regulation will essentially enable (and demand from) regulators that their supervisory activities reach out not only to regulated markets but also to MTFs and OTFs. The Draft Regulation will in principle require that a person’s behaviour may have an impact on financial instruments that are (also) admitted to trading on a regulated market or traded on an MTF or OTF. Yet, it seems that such nexus with a regulated market, MTF or OTF is not always required.[53]

MAD already contains a generous carve-out for Member States, EU central banks, officially designated bodies, and persons acting on their behalf.[54] The Draft Regulation amends the carve-out by explicitly referring to ministries, agencies and special purpose vehicles (such as the EU bailout fund).[55] The question is whether such a broad carve-out is still desired given the current financial and credit crisis in which much inside information is not only produced by issuers but frequently also by EU summits, the ECB, national governments and ministries. It is therefore questionable whether persons acting on behalf of such institutions should be indemnified even if they were to use inside information for their personal benefit.

Under MAD, certain trading behaviour can be qualified as accepted market practice and as such be excluded from the scope of the prohibition on trade-based market manipulation. The Draft Regulation does not allow for this option anymore.

Expansion of supervisory and enforcement powers

The Draft Regulation also expands supervisory and enforcement possibilities for regulators. One of the more significant proposed changes is the provision of access to private

[51] Ibid., Article 2(3). In the case of wholesale energy products, the competent authorities should also take into account the definitions in the Regulation on Wholesale Energy Market Integrity and Transparency. See also I. Diaz-Rainey, J. Ashton and M. Siems, ‘The Financial Regulation of European Wholesale Energy and Environmental Markets’, 19 *Journal of Financial Regulation and Compliance* (2011), p. 355-369.

[52] Draft Regulation, p. 8-9.

[53] See for example Ibid., Article 1(3)(c).

[54] MAD, Article 7.

[55] Draft Regulation, Article 4(1).

premises and telephone and data traffic records from telecom operators.[56] The Commission notes that employing such powers may constitute an interference with certain fundamental rights. For this reason, there should be a reasonable suspicion that the information may be relevant to prove a market abuse case. Also, in the case of access to private premises, there should be prior authorization from the judicial authority in accordance with national law. In the case of access to records, this must not concern the content of the communication but merely the records. For Member States it will probably be easier to provide such powers in relation to criminal investigations than in relation to the employment of supervisory powers. This may require some amendments to national laws dealing with investigatory powers.

Another interesting proposal is the requirement that Member States implement maximum fines which are not too lenient. For individuals the maximum administrative monetary sanctions should be at least EUR 5 million and for legal persons this should be at least 10% of the company's total annual turnover in the preceding business year.[57] In addition, Member States should also allow for the possibility to impose administrative monetary sanctions of (at least) up to twice the amount of the profits gained or losses avoided where those can be determined.[58] Finally, the Draft Directive requires Member States to treat intentional insider dealing and market manipulation as criminal offences, also covering attempt, inciting, aiding and abetting.[59] These proposals clearly signal that Member States will have to make market abuse subject to higher (potential) sanctions.

ESMA will be given a stronger and more active coordinating role. The Draft Regulation stipulates that regulators should cooperate and exchange information (in particular with respect to investigations) with other regulators and ESMA. If a regulator is convinced that market abuse has taken place in another Member State or is affecting financial instruments traded in that other Member State, it should notify the national regulator and ESMA. Also, if market abuse has cross-border effects, ESMA is required to coordinate the investigation if this is requested by one of the national regulators.[60]

So how important are these changes? The Commission proposes modifications to prohibitions and obligations, adjustment of the scope of the market abuse regime and expansion of supervisory and enforcement powers. The urge for regulatory expansion does not come as a surprise. International markets continue to become more interconnected, new financial instruments are being issued and technological developments allow for new types of trading platforms. The transition from 'MAD to MAR' is in that sense evolutionary. However, the Regulation also contains some more revolutionary aspects – at least for practitioners, for instance, the expansion of the scope of the prohibition on insider trading and the definition of attempted market manipulation. Yet, at the same

[56] Ibid., Article 17(2)(e)(f).
[57] Ibid., Article 26(1) (l)(m).
[58] Ibid. Article 26(1) (l)(m).
[59] Ibid., Articles 3 and 4. See also 2., above.
[60] Ibid., Articles 18 and 19.

time, some easy fixes have not been addressed, such as the lack of an explanation of the materiality standard in the prohibition on information-based manipulation.[61]

4. Concerns

The overall tendency of the proposed changes is to increase the level of regulation and harmonization. This is in line with the general lesson learned from the current financial crisis, namely, that financial markets need to be regulated in order to function properly. Yet, it is also important not to have a naïve trust in the effectiveness of legal rules. Research by one of us has shown that the buy-back rules of the EU market abuse law have not had the economic effect that one would have been predicted.[62] Thus, the firm expectation, expressed by the proposals, that the new laws will lead us towards 'economic growth and wealth'[63] seems to be overly confident. Also, given that national regulators will have more markets and instruments to supervise, the effectiveness of the Regulation will depend on the financial means that will be made available by national governments to promote such additional supervision.

As regards the structure of the proposed new market abuse law, the use of a regulation instead of a directive is open to criticism. The first level of the Lamfalussy framework[64] should only provide a general framework, which will then be complemented by more detailed EU legislation at the second level. Therefore, it is not entirely consistent to use a directly applicable legal instrument at the first level. Moreover, the use of a regulation will make market abuse law less transparent for the legal practice. Under the current system, a Member State can implement all first and second level directives as well as national provisions that provide further details in one piece of legislation. In the future, market participants and lawyers will always have to have an eye on both the EU Regulation and national rules, similar to the unsatisfactory structure of the different sets of laws applicable to the European Company (SEs).[65]

With the new law, the prohibitions and obligations will not only be directly applicable but national legislators are also required to allow for criminal enforcement. This means that the prohibitions and obligations need to live up to high quality requirements. The norms should have the quality which one would expect from norms that may be criminally enforced. Yet, it seems that the Commission has not been fully aware of what it requires to formulate such norms, as illustrated by the proposed amendment to the prohibition on insider trading and the definition of attempted manipulation.[66] Poorly defined norms could in practice lead to 'Type I errors' (false positives) or evasion of EU

[61] To be precise the question to what extent immaterial information deficiencies are excluded from this prohibition.
[62] See M. Siems and A. De Cesari, 'The Law and Finance of Share Repurchases in Europe', 35 *Journal of Corporate Law Studies,* (2012), forthcoming.
[63] Draft Regulation, Recital 2; Draft Directive, Recital 1.
[64] See footnote 8, above.
[65] For the latter see, e.g., L. Sasso, 'Societas Europaea: between Harmonization and Regulatory Competition', 4 *European Company Law* (2007), p. 159-167; M. Siems, 'The Impact of the European Company (SE) on Legal Culture', 30 *European Law Review* (2005), p. 431-442.
[66] See Section 3., above.

norms by way of creative judicial interpretations. Both outcomes would be undesirable. The same concerns also apply in relation to administrative enforcement.

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