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THE CODE OF MARKET CONDUCT**Index**

Section 1	Application	2
Section 2	The Regular User Test	5
Section 3	Behaviour	8
Section 4	Misuse of Information	9
Section 5	False or Misleading Impressions	17
Section 6	Distortion	25
Section 7	Statutory Exceptions	30
Section 8	Requiring or Encouraging	32
Section 9	Relationship with Criminal Law and Other Regulatory Requirements	35
Section 10	The Scope of the Market Abuse Regime	36

February 2005

THE CODE OF MARKET CONDUCT

1 APPLICATION

To whom does the Code apply?

- 1.1 The Code of Market Conduct (“the Code”) is made under Section 41B of the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended (“the Law”) which states that “the Commission may prepare and issue a code containing such provisions as the Commission considers will give appropriate guidance to those determining whether or not behaviour amounts to market abuse”. This Code is relevant to all persons seeking guidance as to whether or not behaviour amounts to market abuse.

To what does the Code apply?

- 1.2 Sections 41A to 41H of the Law contain provisions relating to market abuse which are described in this Code as the market abuse regime.
- 1.3 The three tests in the Law (Section 41A(1)) which must be satisfied in order to establish that behaviour, whether by one person alone or by two or more persons jointly or in concert, amounts to market abuse are as follows:
- (1) the behaviour must occur in relation to a qualifying investment traded on a prescribed market [see 10.2 below];
 - (2) the behaviour must satisfy one or more of the three conditions identified in Section 41A(2) of the Law, the text of which is set out below:
 - (a) “the behaviour is based on information which is not generally available to those using the market but which, if available to a regular user of the market, would or would be likely to be regarded by him as relevant when deciding the terms on which transactions in investments of the kind in question should be effected” (Section 41A(2)(a) of the Law);
 - (b) “the behaviour is likely to give a regular user of the market a false or misleading impression as to the supply of, or demand for, or as to the price or value of, investments of the kind in question” (Section 41A(2)(b) of the Law);
 - (c) “a regular user of the market would, or would be likely to, regard the behaviour as behaviour which would, or would be likely to, distort the market in investments of the kind in question” (Section 41A(2)(c) of the Law); and

- (3) the behaviour must be likely to be regarded by a regular user of that market who is aware of the behaviour as a failure on the part of the person or persons concerned to observe the standard of behaviour reasonably expected of a person in his or their position in relation to the market.
- 1.4 Under Section 41F(1) of the Law a person shall, subject to the provisions below, be guilty of an offence and liable on summary conviction, to imprisonment for a term not exceeding six months, or to a fine not exceeding level 5 of the uniform scale, or to both; on conviction on indictment, to imprisonment for a term not exceeding seven years, or to a fine, or to both, where the Court is satisfied that a person (“A”):
- (1) is or has engaged in market abuse; or
 - (2) by taking or refraining from taking any action has required or encouraged another person or persons to engage in behaviour which, if engaged in by A, would amount to market abuse.
- 1.5 In accordance with Section 41F(2) of the Law it shall be a defence for the person “A” to show that there are reasonable grounds for the Court to be satisfied that:
- (1) A believed, on reasonable grounds, that his behaviour did not amount to market abuse; or
 - (2) A had taken all reasonable precautions and exercised all due diligence to avoid engaging in market abuse.
- 1.6 In accordance with Section 41F(2) of the Law it shall be a defence for the person “A” to show that there are reasonable grounds for the Court to be satisfied that:
- (1) A believed, on reasonable grounds, that his behaviour had not required or encouraged another person to engage in behaviour which, if engaged in by the first person, would have amounted to market abuse; or
 - (2) A had taken all reasonable precautions and exercised all due diligence to avoid requiring or encouraging another person to engage in behaviour, which, if engaged in by the first person, would have amounted to market abuse.

Where does the Code apply?

- 1.7 Under Section 41A(5) of the Law, behaviour will fall within the scope of the market abuse regime if it occurs in the Bailiwick, or in relation to qualifying investments traded on a prescribed market which is situated in the Bailiwick or which is accessible electronically in the Bailiwick.

Purpose and Effect

- 1.8 The Code gives guidance for the purpose of determining whether or not behaviour amounts to market abuse, in accordance with Section 41B(1) of the Law.
- 1.9 The Code does not have the effect of modifying or extending any disclosure obligations, including under the Listing Rules of the Channel Islands Stock Exchange, LBG and the Takeover Code or which apply in relation to any prescribed market.
- 1.10 The Code also describes behaviour that, in the Commission's opinion, does not amount to market abuse. Section 41E(1) of the Law (Effect of code) provides that such behaviour is to be taken conclusively, for the purposes of the Law, as not amounting to market abuse. Sections 4.20, 4.21, 4.24, 4.26, 4.28, 5.24, 5.25, 5.27 and 5.28 are referred to in the Code as "safe harbours".
- 1.11 In accordance with Section 41E(2) of the Law, this Code may be taken into account so far as it indicates whether or not behaviour should be taken to amount to market abuse.
- 1.12 The Code is not an exhaustive list of all types of behaviour which may, or may not, amount to market abuse, nor of all the factors to be taken into account in determining whether behaviour amounts to market abuse. The Commission may, subject to the provisions of the Law, alter or replace the Code at any time.

2 THE REGULAR USER TEST

- 2.1 A regular user is defined in Section 41A(10) of the Law as “in relation to a particular market, means a reasonable person who regularly deals on that market in investments of the kind in question.” Behaviour will amount to market abuse only where it would be likely to be regarded by a regular user as a failure on the part of the person or persons concerned to observe the standard of behaviour reasonably expected of a person in his or their position in relation to the market.
- 2.2 In determining whether behaviour amounts to market abuse, it is necessary to consider objectively whether a hypothetical reasonable person, familiar with the market in question, would regard the behaviour as acceptable in the light of all the relevant circumstances.
- 2.3 In determining whether behaviour falls below the standards expected, the regular user is likely to consider all the circumstances of the behaviour, including:
- (1) the characteristics of the market in question, the investments traded on that market, and the users of that market;
 - (2) the rules and regulations of the market in question and any applicable laws. For example, it is likely that it will be relevant to consider the extent to which the behaviour is in compliance with the rules of the particular market and if the person is based overseas it may be relevant to consider the extent to which the behaviour is in compliance with the standards prevailing in that overseas jurisdiction;
 - (3) prevailing market mechanisms, practices and codes of conduct applicable to the market in question;
 - (4) the position of the person in question and the standards reasonably to be expected of that person at the time of the behaviour in the light of that person’s experience, level of skill and standard of knowledge. For example, the standards which it would be reasonable to expect of a retail investor are likely to differ from those to be expected of an industry professional; and
 - (5) the need for market users to conduct their affairs in a manner that does not compromise the fair and efficient operation of the market as a whole or unfairly damage the interests of investors.
- 2.4 The regular user is likely to consider it relevant, although not determinative, that the behaviour conforms with standards that are generally accepted by users of the market. Detailed guidance is given in sections 4 to 6 below as to the different types of behaviour that would not be regarded as acceptable.

- 2.5 The statutory definition of market abuse does not require the person engaging in the behaviour to have intended to abuse the market. Accordingly it is not essential for such an intention or purpose to be present in order for behaviour to fall below the objective standards expected. However, in some circumstances the determination of whether behaviour falls short of those standards will depend on the purpose of the person in question (for example, see 6.4 below). In those circumstances, the regular user is likely to consider the purpose of the person in question in addition to the other relevant considerations listed at 2.3 above. This need not be the sole purpose but should be an actuating purpose.
- 2.6 A mistake is unlikely to fall below the objective standards expected where the person in question has taken reasonable care to prevent and detect the occurrence of such mistakes.
- 2.7 The objective standard of behaviour expected by the regular user is likely to vary to some degree across markets according to the characteristics of the market in question and the investments concerned. For example, the disclosure standards currently expected in equities markets differ from those expected in commodities markets. Consequently, different standards currently apply to the use of non-public information in different markets. Further, the standard expected of a person will vary with the experience, level of skill and standard of knowledge that the regular user is likely to expect from a person in that position. For example, when assessing the standards to be expected of public sector bodies, it is likely that it will be relevant to take into account their statutory and other official functions.
- 2.8 It may often be appropriate to take into account the extent to which the behaviour is in compliance with other applicable rules including the rules of a prescribed market, the Takeover Code or other rules made by the Commission. Compliance with such rules may not be sufficient for the behaviour not to amount to market abuse, since those rules may not be specifically directed at the types of behaviour prohibited by the Law or because compliance with those rules is only one consideration among others. Greater weight is likely to be given to compliance with a rule that expressly requires or permits particular behaviour. However, this will not in itself be determinative. Similarly, failure to comply with a rule will not of itself create a presumption that there has been market abuse. If the prescribed market or the Takeover Panel has granted a dispensation from, or given guidance in advance on, its rules, this is likely also to be a relevant factor in considering whether the behaviour amounts to market abuse.
- 2.9 Where a person's behaviour occurs on an overseas market, but has an impact on a prescribed market, the regular user is likely to consider that it will be relevant to have regard to the local rules, practices and conventions prevailing in the relevant market, and whether or not the person is in the Bailiwick. However, compliance with such rules will not of itself be determinative.
- 2.10 As stated in 2.4 above it is likely to be relevant to consider whether to take into account the extent to which the behaviour conforms with standards that

are generally accepted by users of the market, but again this will not itself be determinative. Such standards will be acceptable where they promote the fair and efficient operation of the market as a whole and do not unfairly damage the interests of investors. In circumstances where there is a range of practices which are generally accepted by users of the market, each practice is to be judged objectively on its own merits.

- 2.11 The Commission does not anticipate that divergences between standards that are generally accepted by users of the market and the standards expected by the regular user will be frequent. In future, the Commission may identify a practice which is accepted in the market, but which, in the Commission's opinion, is likely to fall short of the standards expected by the regular user. In such cases the Commission will consider whether to signal its views on the practice in the form of guidance, or through some other statement, or by revising the Code. The Commission recognises that the former approach will often be more appropriate, and where this is the case the Commission will work with relevant market participants and regulatory bodies to address the causes of concern.
- 2.12 The Commission is satisfied that the rulebooks of the prescribed markets do not permit or require behaviour which amounts to market abuse.
- 2.13 The Code is not exhaustive in its description of behaviour that does or does not amount to market abuse. In circumstances where a person is proposing to undertake an innovative transaction, he should consider it in the light of the guidance provided in sections 4 to 6 below. It is also open to a person to consider seeking guidance from the Commission in respect of the proposed behaviour.

3 BEHAVIOUR

3.1 The types of behaviour which come into the scope of the market abuse regime include, but are not limited to, the following:

- (1) dealing in qualifying investments;
- (2) dealing in commodities or investments which are the subject matter of, or whose price or value is determined by reference to, a qualifying investment (in this case, the commodity will be a “relevant product” in relation to the qualifying investment);
- (3) arranging deals in respect of qualifying investments;
- (4) causing or procuring or advising others to deal in qualifying investments;
- (5) making statements or representations or otherwise disseminating information which is likely to be regarded by the regular user as relevant to determining the terms on which transactions in qualifying investments should be effected;
- (6) providing corporate finance advice and conducting corporate finance activities in qualifying investments; and
- (7) managing investments which are qualifying investments belonging to another.

3.2 Behaviour includes both action and inaction. For example, inaction may amount to market abuse in circumstances where a person is under a legal or regulatory obligation to make a particular disclosure and fails to do so.

4 MISUSE OF INFORMATION

4.1 Statements in this section to the effect that behaviour “amounts to market abuse” assume that the test in 1.3 above has also been met.

4.2 Section 41A(2)(a) of the Law defines behaviour based on misuse of information as:

behaviour which “is based on information which is not generally available to those using the market but which, if available to a regular user of the market, would or would be likely to be regarded by him as relevant when deciding the terms on which transactions in investments of the kind in question should be effected”.

4.3 In all prescribed markets, market users rely on the timely dissemination of such relevant information as they may reasonably expect to receive. Those who possess relevant information ahead of general dissemination should, therefore, refrain from basing their behaviour on that information and from requiring or encouraging others to engage in behaviour until it is disseminated, save in the circumstances set out in 4.20 to 4.30 below. Otherwise, the confidence of market users in the ability of the market to ensure access to such information will be undermined. The extent to which market users may reasonably expect to have access to information differs between different markets. This is explained further below at 4.12 to 4.16.

Behaviour which amounts to market abuse

4.4 Behaviour will amount to market abuse (unless 4.20 to 4.30 below apply) in that it will be a misuse of information where a person deals or arranges deals in any qualifying investment or relevant product where all four of the following circumstances are present:

- (1) the dealing or arranging is based on information. The person must be in possession of information and the information must have a material influence on the decision to engage in the dealing or arranging. The information must be one of the reasons for the dealing or arranging, but need not be the only reason;
- (2) the information must be information which is not generally available. Criteria for determining whether information is generally available are set out in 4.5 below;
- (3) the information must be likely to be regarded by a regular user as relevant when deciding the terms on which transactions in the investments of the kind in question should be effected. Such information is referred to in this Code as “relevant information”. Factors which are to be taken into account when determining whether information is relevant information are set out in 4.9 to 4.11 below;

- (4) the information must relate to matters which the regular user would reasonably expect to be disclosed to users of the particular prescribed market. As explained further below at 4.12 and 4.13 below this includes both matters which give rise to such an expectation of disclosure or are likely to do so either at the time in question, or in the future.

(A) Information which is generally available (4.4(2) above)

4.5 Information is treated as generally available if it can be obtained by research or analysis conducted by, or on behalf of, users of a market (Section 41A(7) of the Law). In addition, information is to be regarded as generally available where one (or more) of the following is satisfied:

- (1) the information has been disclosed to a prescribed market through an accepted channel for dissemination of information or otherwise under the rules of that market;
- (2) the information is contained in records which are open to inspection by the public;
- (3) the information has otherwise been made public, including through the Internet, or some other publication, or is derived from information which has been made public;
- (4) the information can be obtained by observation.

4.6 People are free to use information that they have obtained through research, analysis or other legitimate means. Legitimate means include the observation of a public event. Observation of a public event includes any information which is discussed in a public area or can be observed by the public without infringing rights of privacy, property or confidentiality. Such information will be considered generally available. The fact that in practice other users of the market cannot obtain the information because of limitations in their resources, expertise or competence does not mean that the information cannot legitimately be obtained.

4.7 Examples of information which might be obtainable through legitimate research include:

- (1) information which is available only overseas and has not been published, or otherwise been made available to the public, in the Bailiwick; and
- (2) information which is only available on payment of a fee.

4.8 For example, if a taxi passes a burning factory and a passenger calls his broker using a mobile telephone to sell shares in the factory's owner, that passenger will be acting on information which is generally available, since it is

information which has been obtained by legitimate means through observation of a public event.

(B) Relevant information (4.4(3) above)

4.9 Whether, in a particular case, a particular piece of information would, or would be likely to, be regarded as relevant information by the regular user will depend on the circumstances of the case. In making such determination, the regular user is likely to consider the extent to which:

- (1) the information is specific and precise;
- (2) the information is material;
- (3) the information is current;
- (4) the information is reliable, including how near the person providing the information is, or appears to be, to the original source of that information and the reliability of that source;
- (5) there is other material information which is already generally available to inform users of the market; and
- (6) the information differs from information which is generally available and can therefore be said to be new or fresh information.

4.10 In the case of information relating to possible future developments (which do not currently give rise to an expectation of disclosure (see 4.4(4) above), the following additional factors are to be taken into account when determining the relevance of that information (see example in 4.18 below):

- (1) whether the information provides, with reasonable certainty, grounds to conclude that the possible future developments will, in fact, occur; and
- (2) the significance those developments would assume for market users given their occurrence.

4.11 Examples of relevant information include the following:

- (1) where the qualifying investment in question is issued by a company, or is a derivative relating to a qualifying investment issued by a company, information concerning the business affairs or prospects of the company or a related company;
- (2) where the qualifying investment is a derivative relating to a commodity, information or events affecting the deliverable supply of the commodity, such as, for example, information as to the business operations of major suppliers; and

- (3) information as to official statistics, and fiscal and monetary policy announcements before they are announced.
- (C) **Information which a regular user would reasonably expect to be disclosed to other users of the market (4.4(4) above)**

4.12 Information will only fall within 4.4(4) above if it is either:

- (1) information which has to be disclosed in accordance with any legal or regulatory requirements (referred to as “disclosable information”); or
- (2) information which is routinely the subject of a public announcement although not subject to any formal disclosure requirement (referred to as “announceable information”).

4.13 In the case of information relating to possible future developments (4.4(4) and 4.10 above), which may lead to a disclosure or an announcement being made, the following additional factor is to be taken into account when determining whether the information is to be treated as disclosable information or as announceable information, namely whether the information provides, with reasonable certainty, grounds to conclude that the possible future developments will, in fact, occur and accordingly that a disclosure or announcement will, in fact, be made (see example in 4.18 below).

4.14 Examples of disclosable information include:

- (1) information which is required to be disseminated under the Takeover Code on, or in relation to, qualifying investments traded on a prescribed market;
- (2) information relating to officially listed securities which is required to be disclosed under the Listing Rules

4.15 Examples of announceable information include:

- (1) information which is to be the subject of official announcement by governments, central monetary or fiscal authorities or regulatory body (financial or otherwise, including exchanges);
- (2) changes to published credit rating of companies whose securities are qualifying investments or relevant products; and
- (3) changes to the constituents of a securities index, where the securities are qualifying investments or relevant products.

4.16 Examples of information that would not be announceable information include surveys or research based on information generally available, for example CBI surveys or MORI polls.

(D) Examples

- 4.17 An example of behaviour which falls within 4.4 occurs where a person deals, on a prescribed market, in the equities of XYZ plc, a commodity producer, based on information concerning that company which is not generally available, which is relevant information and which is disclosable or announceable information in relation to the equity market. If the information is also relevant information in relation to a commodity futures contract traded on a prescribed market, dealing in that futures contract based on the information will amount to market abuse only if the information is also disclosable or announceable in relation to the commodity futures market. More generally, where information is required to be disclosed to market A, dealing or arranging deals in qualifying investments traded on A, or in other related products, based on the information will amount to market abuse where this occurs prior to the disclosure being made. Where market A is an equity market, related products will include derivatives and other investments related to the equity in relation to which the disclosure is to be made. Where the information is also relevant to market B, dealing or arranging deals in relation to qualifying investments traded on market B, or in other related products, based on the information will only amount to market abuse where disclosure obligations exist in relation to market B.
- 4.18 An example of information which falls within 4.4(4) arises in connection with the obligation of an officially listed company to announce any major new developments in its sphere of activity which may lead to substantial movement in the price of its listed securities. This could include, for example, entering into a significant contract with a major supplier. In that case, the obligation arises at the time of entering into the contract and disclosure is required to be made without delay. This falls within the category of information set out in 4.4(3) and 4.4(4) above. However, subject to meeting the tests in 4.12 above, the information will fall within 4.4(3) and 4.4(4) above at an earlier stage: namely at the time at which there are grounds to conclude, with reasonable certainty, that the contract will be entered into and that disclosure of the contract will have to be made. Any dealing based on that information in the securities (or investments related to the securities) at that earlier stage would amount to market abuse.

Safe harbours

- 4.19 4.20, 4.21, 4.24, 4.26 and 4.28 each set out descriptions of behaviour that does not amount to market abuse in that the behaviour does not constitute a misuse of information (see 4.4).

(A) Dealing or arranging required for other reasons

- 4.20 Dealing or arranging deals will not amount to a misuse of information if the dealing or arranging was required in order to comply with a legal (including contractual) or regulatory obligation in circumstances where the obligation existed before the relevant information was in the person's possession.

(B) Dealing or arranging not based on information

- 4.21 Dealing or arranging deals will not amount to a misuse of information if the person's possession of relevant information that is not generally available did not influence the decision to engage in the dealing or arranging in question.
- 4.22 It will be presumed for the purposes of 4.21 that the person's possession of the information in question did not influence his decision to deal or arrange deals if:
- (1) the person had taken a firm decision to deal or arrange deals before the relevant information was in the person's possession; and
 - (2) the terms on which the person had proposed to enter into the transaction(s) did not alter after the receipt of the information.
- 4.23 Where a person is an organisation and where one or more individuals within the organisation are in possession of relevant information, it will be presumed for the purposes of 4.21 that such possession had no influence on the person's decision to deal or arrange deals if none of the individuals in possession of the information:
- (1) had any involvement in the decision to engage in the dealing or arranging; or
 - (2) behaved in such a way as to influence, directly or indirectly, the decision to engage in the dealing or arranging; or
 - (3) had any contact with those who were involved in the decision to engage in the dealing or arranging whereby the information could have been transmitted.
- 4.24 Relevant information does not influence the decision to deal or arrange deals if:
- (1) the information in question was held behind an effective Chinese wall and the individual or individuals who dealt or arranged deals was or were on the other side of the Chinese wall; or
 - (2) arrangements equivalent to effective Chinese walls had been established and maintained in respect of the information, and the individuals who dealt or arranged deals did not, therefore, have access to the relevant information.

(C) Trading information

- 4.25 Dealing or arranging deals will not amount to a misuse of information solely because it is based on information as to that person's intention, or any other person's intention, to deal or arrange deals in relation to any qualifying

investment, or information concerning transactions that have taken place. However, this safe harbour does not include dealing or arranging deals:

- (1) based on information as to a possible takeover bid;
- (2) based on information relating to new offers, issues, placements or other primary market activity.

4.26 While dealing or arranging deals which is based on trading information will not constitute market abuse, it may constitute a breach of relevant rules made by the Commission, for example 4.04(f) of the Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998. Specifically 4.26 does not legitimise the front running of customer orders.

(D) Facilitation of takeover bids and other market operations

4.27 Dealing or arranging deals will not amount to a misuse of information if it is engaged in by a person (or someone acting for him) or by another person acting in concert with him in circumstances where:

- (1) the dealing or arranging deals was:
 - (a) in connection with the acquisition or disposal of an equity stake in a company;
 - (b) engaged in for the sole purpose (see 4.29) of making the acquisition or disposal; or
 - (c) where engaged in by a concert party of a person making or potentially making an acquisition or disposal for the sole benefit of that person; and
- (2) the information in question consists of one or more of the following matters:
 - (a) that investments of a particular kind have been or are to be acquired or disposed of, or that their acquisition or disposal is under consideration or the subject of negotiation;
 - (b) that investments of a particular kind have not been or are not to be acquired or disposed of;
 - (c) the number of investments acquired or disposed of, or to be acquired or disposed of, or whose acquisition or disposal is under consideration or the subject of negotiation;
 - (d) the price (or range of prices) at which investments have been, or are to be, acquired or disposed of, or the price (or range of prices) at which the investments whose acquisition or disposal

is under consideration, or the subject of negotiation, may be acquired or disposed of;

- (e) the identity of the person involved, or likely to be involved, in any capacity in an acquisition or disposal;
- (f) in the case of a takeover bid any information legitimately obtained by the bidder in relation to the target company.

4.28 For example, in the context of a takeover bid the following instances of dealing or arranging deals will fall within 4.27:

- (1) seeking from holders of securities irrevocable undertakings or expressions of support to accept an offer to acquire those securities (or not to accept such an offer);
- (2) making arrangements in connection with an issue of securities where those securities are to be offered as consideration for the takeover offer or to be issued in order to fund the takeover offer, including making arrangements for the underwriting or placing of those securities and any associated hedging arrangements by underwriters or placees;
- (3) making arrangements to offer cash as consideration for the takeover offer as an alternative to securities consideration.

4.29 A person should not be prevented from acquiring an equity stake in a company with a view to pursuing a takeover bid or engaging in other forms of market operations simply because he knew that he would be making a bid, and the knowledge amounted to relevant information. For example, a bidder (including a potential bidder), and those who act for him and his associates, may deal in the target company's shares for the purpose of building a stake in the target company or take other steps in connection with a proposed takeover, such as seeking irrevocable undertakings from shareholders or making arrangements for an issue of consideration shares. However, this does not mean that a bidder may undertake any other type of transaction in the target company's shares, or in other investments (for example, contracts for differences or securities of other companies) in relation to which the information is relevant information. For example, a bidder will be engaging in market abuse if he enters into transactions in qualifying investments that provide merely an economic exposure to movements in the price of the target company's shares. Similarly, those who act for the bidder will engage in market abuse if they deal for their own benefit in qualifying investments or relevant products in respect of which information concerning the proposed bid is relevant information. (See 8.3, 8.7(2) and 8.8 below).

(E) Underwriting agreements

4.30 Agreeing to underwrite an issue of securities will not of itself amount to a misuse of information.

5 FALSE OR MISLEADING IMPRESSIONS

Introduction

- 5.1 Statements in this section to the effect that behaviour “amounts to market abuse” assume that the test in 1.3(1) has also been met.
- 5.2 Section 41A(2)(b) of the Law defines behaviour giving rise to a false or misleading impression as follows:

behaviour which “is likely to give a regular user of the market a false or misleading impression as to the supply of, or demand for, or as to the price or value of, investments of the kind in question”.

- 5.3 Prescribed markets provide a mechanism by which the price or value of investments may be determined according to the market forces of supply and demand. When market users trade on prescribed markets they expect the price or value of investments and volumes of trading to reflect the proper operation of market forces rather than the outcome of improper conduct by other market users. Improper conduct which gives market users a false or misleading impression results in market users no longer being able to rely on the prices formed in markets or volumes of trading as a basis for their investment decisions. This will undermine confidence in the integrity of the prescribed market and overall market activity may decrease and transaction costs may rise, or both, to the detriment of market users, including investors.

Elements of the test

- 5.4 In order to fall within the false or misleading impressions test:
- (1) the behaviour must be likely to give the regular user a false or misleading impression. Behaviour will amount to market abuse if the behaviour engaged in is likely to give rise to, or to give an impression of, a price or value or volume of trading which is materially false or misleading; and
 - (2) in order to be likely, there must be a real and not fanciful likelihood that the behaviour will have such an effect, although the effect need not be more likely than not. The behaviour may, or may be likely to, give rise to more than one effect, including the effect in question.

General factors

- 5.5 Factors that are to be taken into account in determining whether or not behaviour is likely to give the regular user a false or misleading impression as to the supply of, or the demand for, or the price or value of a qualifying investment or relevant product include:
- (1) the experience and knowledge of the users of the market in question;

- (2) the structure of the market, including its reporting, notification and transparency requirements;
- (3) the legal and regulatory requirements of the market concerned and accepted market practices;
- (4) the identity and position of the person responsible for the behaviour which has been observed (if known); and
- (5) the extent and nature of the visibility or disclosure of the person's activity.

Relationship with distortion

- 5.6 In some circumstances, behaviour which falls within these descriptions (see 5.7) may also fall within the descriptions of behaviour giving rise to a market distortion (see section 6 below).

Behaviour which amounts to market abuse

- 5.7 5.8, 5.15, 5.18 and 5.21 each set out descriptions of behaviour that amount to market abuse in that the behaviour gives rise, or is likely to give rise, to a false or misleading impression.

(A) Artificial transactions

- 5.8 Behaviour will constitute market abuse where:

- (1) a person enters into a transaction or series of transactions in a qualifying investment or relevant product; and
- (2) the principal effect of the transaction or transactions will be, or will be likely to be, to inflate, maintain or depress the apparent supply of, or the apparent demand for, or the apparent price or value of a qualifying investment or relevant product so that a false or misleading impression is likely to be given to the regular user; and
- (3) the person knows or could reasonably be expected to know, that the principal effect of the transaction or transactions on the market will be, or will be likely to be, as set out as 5.8(2);

unless the regular user would regard:

- (4) the principal rationale for the transaction in question as a legitimate commercial rationale; and
- (5) the way in which the transaction is to be executed as proper.

- 5.9 A transaction which creates a false or misleading impression will not normally be considered to have a legitimate commercial rationale where the purpose behind the transaction was to induce others to trade in, or to position or move the price of, a qualifying investment or relevant product. This need not be the sole purpose for entering into the transaction or transactions, but must be an actuating purpose. Equally, transactions will not automatically be considered to have a legitimate commercial rationale simply because the purpose behind the transaction was to make a profit or avoid a loss (whether directly or indirectly).
- 5.10 A transaction will be executed in a proper way where it is executed in a way which takes into account the need for the market as a whole to operate fairly and efficiently. The way in which a transaction was executed would be unlikely to be regarded as proper by the regular user where a transaction was executed in a particular way with the purpose of creating a false or misleading impression. In most cases the rules of prescribed markets include a requirement that transactions be executed in a proper way (for example, rules on reporting and executing cross-transactions). Transactions would not necessarily be considered to have been executed in an improper way simply because the way in which they were executed did not disclose the firm's intentions or positions to the market.
- 5.11 The following factors are to be taken into account when determining whether a person's behaviour amounts to market abuse as described in 1.5.8 above, although the presence of one or more of these factors does not automatically mean the behaviour in question amounts to market abuse:
- (1) whether the transaction causes or contributes to an increase (or decrease) in the supply of, or the demand for, or the price or value of a qualifying investment or relevant product and the person has an interest in the level of the supply of, or the demand for, or the price or value of the qualifying investment or relevant product;
 - (2) whether the transaction involves the placing of buy and sell orders at prices higher or lower than the market price, or the placing of buy and sell orders which increase the volume of trading;
 - (3) whether the transaction coincides with a time at or around which the supply of, or the demand for, or the price or value of a qualifying investment or relevant product is relevant (whether for the market as a whole or the person in question) to the calculation of reference prices, settlement prices, and valuations (for example, close of trading, end of quarter);
 - (4) whether those involved in the transaction are connected parties;
 - (5) whether the transaction causes the market price of an investment in question to increase or decrease, following which the market price immediately returns to its previous level;

- (6) whether a person places a bid (or offer) which is higher (or lower) than the previous bid (or offer) only to remove the bid (or offer) from the market before it is executed.
- 5.12 A further factor to be taken into account in determining whether the behaviour amounts to market abuse as described in 5.8 above is the extent to which the transaction generally either opens a new position, so creating an exposure to market risk, or closes out a position and so removes market risk. This factor, if present, will tend to suggest that the transaction is likely to have a legitimate commercial rationale and the behaviour does not amount to market abuse as described in 5.8, subject to the way in which the transaction is executed. Examples of transactions which typically have a legitimate commercial rationale are given at 5.24 below.
- 5.13 A person has an interest in a qualifying investment or relevant product where that person:
- (1) may directly (including by holding a short position) or indirectly benefit from alterations in its market price; or
 - (2) may be rewarded by, or is otherwise in collusion with or connected with, persons who may benefit from alterations in the market price of the qualifying investment.
- 5.14 Examples of behaviour which might give rise to a false or misleading impression and in respect of which the principal rationale may not be a legitimate commercial rationale include:
- (1) arrangements for the sale or purchase of a qualifying investment or relevant product (other than on repo or on stock lending or borrowing terms) whereby there is no change in beneficial interests or market risk, or the transfer of beneficial interest or market risk is only between persons who are acting in concert or collusion;
 - (2) a transaction or series of transactions that are designed to conceal the ownership of a qualifying investment or relevant product, so that disclosure requirements are circumvented by the holding of the qualifying investments in the name of a colluding party, such that disclosures are misleading in respect of the true underlying holding of the security. These transactions are often structured so that market risk remains with the seller. This does not include nominee holdings;
 - (3) a fictitious transaction.
- (B) Disseminating information**
- 5.15 Behaviour will constitute market abuse where:
- (1) a person disseminates information which is, or if true would be, relevant information;

- (2) the person knows, or could reasonably be expected to know, that the information disseminated is false or misleading; and
- (3) the person disseminates the information in order to create a false or misleading impression (this need not be the sole purpose for disseminating the information, but must be an actuating purpose).

5.16 A factor to be taken into account in determining the purpose of the person in question is whether that person has an interest in a qualifying investment or relevant product (see 5.13) to which the information is relevant. This factor, if present, will tend to suggest that the person had disseminated the information in order to create a false or misleading impression. That said, the absence of any such interest does not conclusively demonstrate that the behaviour does not amount to market abuse.

Examples

5.17 The following is an example of disseminating false or misleading information. A person posts information on an Internet bulletin board or chat room which contains false or misleading statements about the takeover of a company whose shares are qualifying investments. The person knows that the information is false or misleading and he has posted the information in order to create a false or misleading impression.

(C) Dissemination of information through an accepted channel

5.18 Behaviour will constitute market abuse where:

- (1) a person responsible for the submission of the information to an accepted channel for the dissemination of information submits information which is, or if true would be, relevant information which is likely to give the regular user a false or misleading impression as to the supply of, or the demand for, or the price or value of a qualifying investment or relevant product; and
- (2) the person who submits the information has not taken reasonable care to ensure it is not false or misleading.

5.19 There are a number of channels through which information relating to qualifying investments which are traded on prescribed markets is formally disseminated to other market users. Some information is required to be disseminated through one of these channels, for example, under the rules of the prescribed market or the Listing Rules. Investment exchanges also use these channels to disseminate information about trades which have been executed on their markets.

5.20 The Commission recognises the importance of information disseminated through accepted channels for the dissemination of information. Users of such information should be able to rely on the accuracy and integrity of information

carried through these channels. It is, therefore, appropriate that those who disseminate information through them, for example, the company itself, its financial advisers or its public relations advisers, take reasonable care to ensure the information is not inaccurate or misleading. Where they do not, and the information is likely to give rise to a false or misleading impression, they will be regarded as engaging in behaviour which amounts to market abuse.

(D) Course of conduct

5.21 Behaviour will constitute market abuse where:

- (1) a person engages in a course of conduct, the principal effect of which will be, or is likely to be, to give a false or misleading impression to the regular user as to the supply of, or the demand for, or the price or value of a qualifying investment or relevant product; and
- (2) the person knows, or could reasonably be expected to know, that the principal effect of the conduct on the market will be, or is likely to be as set out in 5.21(1);

unless the regular user would regard:

- (3) the principal rationale for the conduct in question as a legitimate commercial rationale (see 5.9 above) and
- (4) the way in which the conduct is engaged in as proper (see 5.10 above).

Examples

5.22 The exact nature of conduct that might give a false or misleading impression will vary according to the characteristics of the market. The following are examples of behaviour which might give a false or misleading impression to the regular user:

- (1) the movement of physical commodity stocks, which might create a misleading impression as to the supply of, or demand for, or price or value of, a commodity or the deliverable into a commodity futures contract; and
- (2) the movement of an empty cargo ship, which might create a false or misleading impression as to the supply of, or the demand for, or the price or value of a commodity or the deliverable into a commodity futures contract.

Safe harbours

5.23 5.24, 5.25, 5.27 and 5.28 each set out descriptions of behaviour that does not amount to market abuse in that the behaviour does not give rise to a false or misleading impression (see 5.4 above).

(A) Permitted transactions

5.24 The following examples of behaviour will not give rise to a false or misleading impression even though the conditions described in 5.8(1), 5.8(2) and 5.8(3) are satisfied, provided that the conditions in 5.8(4) and 5.8(5) are also satisfied:

- (1) transactions which effect the taking of a position, or the unwinding of a position taken, so as to take legitimate advantage of:
 - (a) differences in the taxation of income or capital returns generated by investments or commodities (whether such differences arise solely because of the identity of the person entitled to receive such income or capital or otherwise); or
 - (b) differences in the prices of investments or commodities as traded in different locations; or
- (2) transactions which effect the lending or borrowing of qualifying investments or commodities so as to meet an underlying commercial demand for the investment or commodity.

(B) Required reporting or disclosure of transactions

5.25 Making a report or disclosure will not, of itself, give rise to a false or misleading impression if:

- (1) the report or disclosure was made in accordance with the way specified by any applicable legal or regulatory requirement; and
- (2) the report or disclosure was expressly required or expressly permitted by the rules of a prescribed market or the rules of the Takeover Code or by any other applicable law, ordinance or regulation or the rules of any competent statutory, governmental or regulatory authority.

(C) Chinese walls

5.26 Where a person is an organisation, that person may be aware of information that is not known to all of the individuals within the organisation. If an individual within the organisation disseminates information which he would know, or could reasonably be expected to know, is false or misleading if he was aware of information held by other individuals within the organisation, then that person will be taken not to know, or to be reasonably expected to know, that the information disseminated was false or misleading if:

- (1) the other information in question is held behind an effective Chinese wall or is restricted using other similarly effective arrangements; and

- (2) there was nothing which was known, or ought reasonably to have been known, to the individual who disseminated the information which should have led him to conclude it was false or misleading.
- 5.27 For the purposes of 5.26, the fact that the person did not know, or could not be reasonably expected to know, that the information was false or misleading can be demonstrated by showing that the requirements identified in 4.22 above have been satisfied. Where it can be demonstrated that the individual disseminating the information did not know, or could not be reasonably expected to know, that the information was false or misleading, behaviour will not fall within the description of market abuse set out in 5.15 above.
- 5.28 The circumstances described in 4.23(1) to 4.23(3) are capable of giving rise to a presumption that the other information in question is held behind an effective Chinese wall or is restricted using other similarly effective arrangements.

6 DISTORTION

Introduction

6.1 Statements in this section to the effect that behaviour “amounts to market abuse” assume that the test in 1.3(1) above has also been met.

6.2 Section 41(A)(2)(c) of the Law defines behaviour amounting to distortion as follows:

“a regular user of the market would, or would be likely to, regard the behaviour as behaviour which would, or would be likely to, distort the market in investments of the kind in question.”

6.3 The matters in 5.3 above apply with equal force in connection with behaviour which gives rise to market distortion. A person may not engage in behaviour that interferes with the proper operation of market forces and so with the interplay of proper supply and demand and so has a distorting effect. Distortion undermines confidence in the prescribed markets and damages efficiency to the detriment of market users, including investors.

Elements of the test

6.4 In order to fall within the distortion test:

(1) the *behaviour* must be such that a regular user would, or would be likely to, regard it as behaviour which would, or would be likely to, distort the market in the investment in question. Behaviour will amount to market abuse if the behaviour engaged in interferes with the proper operation of market forces with the purpose of positioning prices at a distorted level. This need not be the sole purpose of entering into the transaction or transactions, but must be an actuating purpose; and

(2) in order to be likely, there must be a real and not fanciful likelihood that the behaviour will have such an effect, although the effect need not be more likely than not. The behaviour may, or may be likely to, give rise to more than one effect, including the effect in question.

6.5 It is unlikely that the behaviour of market users when trading at times and in sizes most beneficial to them (whether for the purpose of long term investment objectives, risk management or short term speculation) and seeking the maximum profit from their dealings will of itself amount to distortion. Such behaviour, generally speaking, improves the liquidity and efficiency of markets.

6.6 It is unlikely that prices in the market which are trading outside their normal range will necessarily be indicative that someone has engaged in behaviour with the purpose of positioning prices at a distorted level. High or low prices

relative to a trading range can be the result of the proper interplay of supply and demand.

Relationship with false or misleading impressions

- 6.7 In some circumstances, behaviour which falls within these descriptions (see 6.8 below) may also fall within the scope of the prohibition against behaviour giving rise to a false or misleading impression (see Section 5 above).

Behaviour which amounts to market abuse

- 6.8 6.9 and 6.13 below each set out descriptions of behaviour that amount to market abuse in that the behaviour gives rise to market distortion.

(A) Price positioning

- 6.9 Behaviour will constitute market abuse where a person enters into a transaction, or a series of transactions, with the purpose of positioning the price of a qualifying investment or relevant product at a distorted level (the purpose need not be the sole purpose for entering into the transaction or transactions, but must be an actuating purpose).
- 6.10 It follows that behaviour which incorporates a purpose of positioning the price at a distorted level cannot have a legitimate commercial rationale. The Code does not restrict market users trading significant volumes where there is a legitimate purpose for the transaction (for example, index tracking which can involve trading significant volumes on the close) and where the transaction is executed in a proper way, that is, a way which takes into account the need for the market as a whole to operate fairly and efficiently. In most cases the rules of prescribed markets include a requirement that transactions be executed in a proper way (for example, rules on reporting and executing cross-trades). Such behaviour is unlikely to distort the market in the investments in question, even if it causes the market to move. But trading significant volumes with the purpose of controlling the price of a qualifying investment or a relevant product and positioning it at a distorted level will amount to market abuse.
- 6.11 The following factors will be taken into account when determining whether a person has positioned the price of a qualifying investment or relevant product at a distorted level, although the presence of one or more of these factors does not automatically mean the market has been distorted:
- (1) the extent to which the timing of the person's transaction or transactions coincided with a time at or around which the price of the qualifying investment or relevant product was relevant (whether for the market as a whole and or the person in question) to the calculation of reference prices, settlement prices, and valuations (for example, close of trading, end of quarter);
 - (2) the extent to which the person had a direct or indirect interest in the price or value of the qualifying investment or relevant product;

- (3) the volume or size of the person's transaction or transactions in relation to reasonable expectations of the depth and liquidity of the market at the time in question;
- (4) the extent to which price, rate or option volatility movements, and the volatility of these factors for the investment in question occur which are outside their normal intra-day, daily, weekly or monthly range;
- (5) the extent to which the person's transaction or transactions caused the market price of the investment to increase or decrease, following which the market price returned immediately to its previous level; and
- (6) whether a person has successively and consistently increased or decreased his bid, offer or the price he has paid for a qualifying investment or relevant product.

Examples

6.12 The following are examples of price positioning at a distorted level:

- (1) a trader simultaneously buys and sells the same investment (that is, trades with himself) to give the appearance of a legitimate transfer of title or risk (or both) at a price outside the normal trading range for the investment. The price of the investment is relevant to the calculation of the settlement value of an option. He does this while holding a position in the option. His purpose is to position the price of the investment at a distorted level, making him a profit or avoiding a loss;
- (2) a trader buys a large volume of commodity futures (whose price will be relevant to the calculation of the settlement value of a derivatives position he holds) just before the close of trading. His purpose is to position the price of the commodity futures at a distorted level so as to make a profit from his derivatives position;
- (3) a trader holds a short position that will show a profit if a particular investment, which is currently a component of an index, falls out of that index. The question of whether the investment will fall out of the index depends on the closing price of the investment. He places a large sell order in the investment just before the close of trading. His purpose is to position the price of the investment at a distorted level so that the investment will drop out of the index so as to make a profit; and
- (4) a fund manager's quarterly performance will improve if the valuation of this portfolio at the end of the quarter in question is higher rather than lower. He places a large order to buy relatively illiquid shares, which are also components of his portfolio, to be executed at or just before the close. His purpose is to position the price of the shares at a distorted level.

(B) Abusive squeezes

6.13 Behaviour will constitute market abuse where a person engages in an abusive squeeze. That is, where a person with:

- (1) a significant influence over the supply of, or demand for, or delivery mechanisms for a qualifying investment or relevant product; and
- (2) a position (directly or indirectly) in an investment under which quantities of the qualifying investment or relevant product in question are deliverable;

engages in behaviour with the purpose of positioning at a distorted level the price at which others have to deliver, take delivery or defer delivery to satisfy their obligations (the purpose need not be the sole purpose of entering into the transaction or transactions, but must be an actuating purpose).

6.14 Squeezes occur relatively frequently when the proper interaction of supply and demand leads to market tightness, but this is not of itself abusive. In addition, having a significant influence over the supply of, or demand for, or delivery mechanisms for an investment, for example, through ownership, borrowing or reserving the investment in question, is not of itself abusive.

6.15 An abusive squeeze occurs when a person has satisfied the conditions in 6.13, which include positioning the price at a level materially different than the price that would have been determined by the interaction of proper supply and demand at which others have to deliver, take delivery or defer delivery to satisfy their obligations. Abusive squeezes damage liquidity and confidence in prescribed markets on a multilateral, not just a bilateral, basis and damage confidence in the delivery mechanisms of prescribed markets.

6.16 The following factors will be taken into account when determining whether a person has engaged in an abusive squeeze. These factors do not impose new obligations on market users. For example, they do not impose an obligation to lend to others where one does not already exist, although behaviour is less likely to amount to an abusive squeeze if a person is willing to lend the investment in question. The factors are as follows:

- (1) the extent to which a person is willing to relax his control or other influence in order to help maintain an orderly market, and the price at which he is willing to do so;
- (2) the extent of which the person's activity causes, or risks causing, settlement default by other market users on a multilateral basis and not just a bilateral basis. The more widespread the risk of multilateral settlement default, the more likely that the market has been distorted;
- (3) the extent to which prices under the delivery mechanisms of the market diverge from the prices for delivery of the investment or its equivalent

outside those mechanisms. The greater the divergence beyond that to be reasonably expected, the more likely that the market has been distorted; and

- (4) the extent to which the spot or immediate market compared to the forward market is unusually expensive or inexpensive or the extent to which borrowing rates are unusually expensive or inexpensive.

6.17 The effects of an abusive squeeze are likely to be influenced by the extent to which other market users have failed to protect their own interests or fulfil their obligations in a manner consistent with the standards of behaviour to be expected of them in that market. The regular user is likely to expect other market users to settle their obligations and not to put themselves in a position where, to do so, they have to rely on holders of long positions lending when they may not be inclined to do so and may be under no obligation to do so.

Examples

6.18 The following is an example of an abusive squeeze. A trader with a long position in bond futures buys or borrows a large amount of the cheapest to deliver bonds and either refuses to re-lend these bonds or will only lend them to parties he believes will not re-lend to the market. His purpose is to position the price at which those with short positions have to deliver to satisfy their obligations at a materially higher level, making him a profit.

7 STATUTORY EXCEPTIONS

7.1 The Law provides statutory exceptions for the two types of behaviour in relation to the market abuse regime. The first relates to behaviour which is described in this Code as not amounting to market abuse (see 1.10 above). The second relates to behaviour which conforms with relevant rules or guidance made by the Commission (Section 41A(8) of the Law). In the Code, specific instances of both these exceptions are referred to as “safe harbours”. In addition, the Law states that information which can be obtained by research or analysis is to be regarded as generally available (Section 41A(7) of the Law) (see 4.5 above).

7.2 Behaviour will be regarded as conforming with a rule made by the Commission only if it is required or expressly permitted by that rule. In order to fall within this safe harbour, there must be a specific rule that either requires or expressly permits a person to engage in the behaviour in question.

Rules made by the Commission

7.3 Section 41A(8) of the Law states:

“Behaviour does not amount to market abuse -

- (a) if it conforms with –
 - (i) price stabilising rules made by the Commission; or
 - (ii) guidance issued by the Commission on the management of conflicts of interests; and
- (b) the rules or guidance include a provision to the effect that behaviour conforming with the rule or (as the case may be) the guidance does not amount to market abuse.”

City Code on Takeovers and Mergers (“the City Code”)

7.4 Under the provisions of Section 41C(1) of the Law the Commission may include in a code issued by it under Section 41B of the Law provision to the effect that in its opinion behaviour conforming with the City Code or with any other code or guidance issued in relation to takeovers and mergers issued in any other jurisdiction-

- (a) does not amount to market abuse;
- (b) does not amount to marker abuse in specified circumstances; or
- (c) does not amount to market abuse if engaged in by a specified description of person.

7.5 The Law also requires the Commission to keep itself informed of the way in which-

- (a) in the case of the City Code, the Panel on Takeovers and Mergers;
- (b) in the case of a code or guidance issued in another jurisdiction, the body in that jurisdiction charged with the administration of that code or guidance;

interprets and administers the relevant provisions of the City Code or (as the case may be) that code or guidance.

7.6 The City Code applies to offers and other specified transactions for all listed and unlisted public companies considered by the Panel on Takeovers and Mergers to be resident in the United Kingdom, the Channel Islands or the Isle of Man. The City Code does not apply to open-ended investment companies. The Panel on takeovers and Mergers will normally consider a company to be resident only if it is incorporated in the United Kingdom, the Channel Islands or the Isle of Man and has its place of central management in one of those jurisdictions.

7.7 In respect of offers and transactions relating to companies that are not resident in the United Kingdom, the Channel Islands or the Isle of Man the Commission considers it appropriate to consider any applicable code or guidance issued by the authorities in the country of incorporation of the subject company, or where necessary, the country in which the company's shares are listed. In the absence of such guidance or code the Commission may consider whether the City Code offers any appropriate guidance.

8 REQUIRING OR ENCOURAGING

8.1 Section 41F(1)(b) of the Law gives the Court the power to impose a penalty on a person, “A”, if it is satisfied that A, “by taking or refraining from taking any action has required or encouraged another person or persons to engage in behaviour which, if engaged in by A, would amount to market abuse”.

8.2 For the purposes of section 41F(1)(b) it must be shown:

- (1) that the behaviour would have amounted to market abuse if carried out by the person who requires or encourages (to which hypothetical situations the principles set out in this Code will be applied); and
- (2) that the person, by action or inaction, required or encouraged another to engage in the behaviour in question.

It is not necessary to show that the person who requires or encourages has benefited from the action of the person who is required or encouraged.

8.3 There are many ways in which a person, A, may, by taking or refraining from taking any action, require or encourage another person, B, to engage in behaviour which, if engaged in by A, would amount to market abuse. Some examples of behaviour that might fall within the scope of Section 41F(1)(b) are as follows:

- (1) where a director of a company, while in possession of information which is both relevant information and disclosable information (other than trading information) and which is not generally available to market users, instructs an employee of that company to deal in qualifying investments or relevant products in respect of which the information is relevant and disclosable information;
- (2) where A recommends or advises B to engage in behaviour which, if engaged in by A, would amount to market abuse.

8.4 Whether a person’s taking or refraining from taking action might be regarded as requiring or encouraging others will depend on circumstances such as acceptable market practices, the experience, level of skill and standard of knowledge of the person concerned, and the control or influence the person has in relation to the person who engages in the behaviour in question.

8.5 However, early or selective disclosure of information which a regular user would expect market users to have will generally be presumed to constitute requiring or encouraging unless there is a legitimate purpose for making the disclosure, for example, as permitted or required by the rules of a prescribed market, the rules made by the Commission, or the rules of the Takeover Code. Any such disclosure should be accompanied by a statement at or before the time the information is passed that the information is given in confidence and that the recipient should not base any behaviour in relation to the qualifying investment or relevant product which would amount to market abuse on the

information until after the information is made generally available. Such a statement may be incorporated in the express or implied terms of any contract governing the relationship between the persons making and receiving the disclosure. Some examples of disclosure for a legitimate purpose are set out in 8.6.

8.6 The Commission will not regard a person as requiring or encouraging others to deal if he passes information which is relevant information and not generally available to:

- (1) his employees (or, where appropriate, his fellow employees or employees of a group or associated company) for the purpose of enabling them to perform their functions in circumstances where the possession of the information in question is necessary for the proper performance of those functions; or
- (2) his professional advisers, and or the professional advisers of any persons involved or who may be involved in any transaction or takeover bid with or involving him, for the purpose of obtaining advice; or
- (3) any person with whom he is negotiating, or intends to negotiate, any commercial, financial or investment transaction (including prospective underwriters or placees of securities) for the purpose of facilitating the proposed transaction; or
- (4) any person from whom he is seeking or intends to seek an irrevocable commitment or expression of support in relation to an offer which is subject to the Takeover Code, for the purpose of obtaining that commitment or expression of support; or
- (5) representatives of his employees or trade unions acting on their behalf in fulfilment of a legal obligation; or
- (6) any department of the States of Guernsey, the Takeover Panel or any other statutory or regulatory body or authority for the purposes of fulfilling a legal and regulatory obligation or otherwise in connection with the performance of the functions of the body to which the information has been passed.

8.7 In the context of a takeover bid (see 4.28 to 4.30 above), a person, A, will not be regarded as having required or encouraged another person, B, to engage in behaviour amounting to market abuse in circumstances where:

- (1) A is an adviser to B, and B is considering the acquisition or disposal of an equity stake; and
- (2) A advises B to acquire or dispose of an equity stake in the target company for the purposes and in the manner specified in 4.28.

- 8.8 Where the originator of the transaction appears to have engaged in market abuse and, in the course of doing so, has acted through an intermediary, the intermediary's behaviour will not amount to either requiring or encouraging or market abuse unless the intermediary knew or ought reasonably to have known that the originator was engaging in market abuse.
- 8.9 There are circumstances where the Commission will regard a person as requiring or encouraging; for example, where a person who has relevant and disclosable information about a company which is not yet generally available to other market users, advises or encourages another to acquire shares in that company, unless guidance suggests that this is acceptable (see for example, 8.7).

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9 RELATIONSHIP WITH CRIMINAL LAW AND OTHER REGULATORY REQUIREMENTS

- 9.1 Nothing in the Code makes lawful or permits any activity that contravenes the criminal law or applicable legal or regulatory requirements. In particular, nothing in the Code modifies or affects any other obligations of persons who are bound by rules made by the Commission, the rules of a prescribed market or other relevant rules, regulations or codes of conduct or good practice.
- 9.2 Persons will, therefore, need to ensure that, even if their behaviour does not amount to market abuse, it does not breach:
- (1) any applicable criminal law, for example the insider dealing provisions of the Company Securities (Insider Dealing)(Bailiwick of Guernsey) Law, 1996 as amended; or
 - (2) any applicable rules made by the Commission, for example the relevant sections of the Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998; or
 - (3) any other legal or regulatory requirements to which they are subject, including the rules and regulations of prescribed markets, the provisions of the Takeover Code, Guernsey Company Law, any applicable overseas rules and regulatory requirements.
- 9.3 Principle 7 of Schedule 2 to the Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998 requires licensees to observe high standards of market conduct. There is, therefore, some degree of overlap between the aforementioned Principle 7 and the market abuse regime. However, there are some important differences:
- (1) Principle 7 applies only to persons, licensed under the Protection of Investors (Bailiwick of Guernsey) Law, 1987 as amended, regulated by the Commission, whereas the market abuse regime applies to all persons.
 - (2) The market abuse regime applies only to behaviour, which occurs in relation to qualifying investments traded on a prescribed market. Principle 7 applies, in respect of licensees, in relation to activities wherever conducted.
 - (3) Principle 7 is broader in scope than the market abuse regime. Principle 7 is directed generally at all behaviour, which may fall short of proper standards of market conduct. Accordingly, behaviour may fall short of proper standards of market conduct, and breach Principle 7, even though such behaviour does not constitute market abuse.

10 THE SCOPE OF THE MARKET ABUSE REGIME

Prescribed markets and qualifying investments

- 10.1 Section 41A(1) of the Law defines market abuse as behaviour which amongst other things

“occurs in relation to qualifying investments traded on a market to which this section applies”.

- 10.2 Section 41A(3) allows the States of Guernsey Policy Council (or such other Committee or body as the States of Guernsey may specify by Ordinance) to prescribe, by regulations, markets and qualifying investments.

The prescribed markets are those markets specified in the Orders made under 9(1) of the Company Securities (Insider Dealing) (Bailiwick of Guernsey) Law, 1996. *(Regulations will need to be made)*

The “qualifying investments” are those investments that fall within the scope of the definition of Controlled Investment set out in Schedule 1 to the Law. For the avoidance of doubt, such qualifying investments include Category 1 controlled investments; that is open-ended collective investments schemes and Category 2 controlled investments, that is general securities and derivatives. *(Regulations will need to be made)*

- 10.3 In the majority of cases, there will be no dispute that an investment is “traded on” a prescribed market. However, in a small number of cases, for example, where an investment has traded in the past but not recently, and where an investment has not yet started trading, the answer may be less obvious. To avoid any doubt, the following investments would be “traded on” a prescribed market:

- (1) investments which have not yet traded subject to the rules of a prescribed market from the point they start trading subject to the rules of a prescribed market (including the first trade);
- (2) investments which are currently trading subject to the rules of a prescribed market; and
- (3) investments which have traded in the past and can still be traded subject to the rules of a prescribed market.

- 10.4 The fact that behaviour has occurred in relation to an investment “traded on” a prescribed market is a necessary condition for market abuse to have occurred but it is not a sufficient condition. In addition, the behaviour must, among other things, satisfy one or more of the three conditions identified in section 41A(2) of the Law. It is difficult to see how these tests could be satisfied where there is no ongoing market on the prescribed market in the qualifying investment. If there is no ongoing market for a qualifying investment on a prescribed market, market participants are unlikely to rely on the prescribed

market for price discovery or price formation. Equally, any trading in such a qualifying investment that is not associated with the prescribed market is unlikely to damage confidence in the prescribed market. The question of whether there is an ongoing market will depend on a number of factors, including how recently and in what volumes the qualifying investment has traded. The importance of these factors is likely to vary from market to market.

- 10.5 An example shows how this guidance might be applied. An investment has not traded for a long time or only in insignificant volumes but it can still be traded subject to the rules of a prescribed market. The investment will be “traded on” a prescribed market for the purposes of the regime (see 10.3 above). There will probably be no ongoing market in this investment since it has not traded for a long time or only in insignificant volumes. For that reason, behaviour in the investment is unlikely to amount to market abuse (10.4 above).
- 10.6 Section 41A(1)(a) of the Law requires that, in order to amount to market abuse, behaviour must occur in relation to qualifying investments traded on a market to which the section applies. According to section 41A(6) of the Law:
- “the behaviour which is to be regarded as occurring in relation to qualifying investments includes behaviour which:
- (1) occurs in relation to anything which is the subject matter, or whose price or value is expressed by reference to the price or value, of those qualifying investments; or
 - (2) occurs in relation to investments (whether qualifying or not) whose subject matter is those qualifying investments.”
- 10.7 The definition of behaviour in relation to a qualifying investment in section 41A(6) of the Law is not exhaustive. However, there must be a clear relationship between the behaviour and a qualifying investment for the behaviour to be regarded as occurring in relation to a qualifying investment. Further, where behaviour is engaged in for the purpose of abuse in relation to a qualifying investment, it may be regarded as having occurred in relation to a qualifying investment even though the behaviour is not in a qualifying investment or relevant product (see 10.8 below).
- 10.8 The statutory definition of behaviour which occurs in relation to qualifying investments set out at 10.6 above includes behaviour in relation to other investments which are not themselves qualifying investments, since such behaviour can have a damaging effect on confidence in prescribed markets and qualifying investments. These related investments are referred to in this Code as relevant products.

10.9 Behaviour in the following relevant products is caught by section 41A(6) of the Law:

- (1) anything that is the subject matter of a qualifying investment;
- (2) anything whose price is expressed by reference to the price of a qualifying investment;
- (3) anything whose price is expressed by reference to the value of a qualifying investment;
- (4) anything whose value is expressed by reference to the price of a qualifying investment;
- (5) anything whose value is expressed by reference to the value of a qualifying investment;
- (6) investments (whether qualifying or not) whose subject matter is a qualifying investment.

February 2005