Europe Economics

Data Gathering and Cost Analysis on Draft Technical Standards Relating to the Market Abuse Regulation

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1 Executive Summary

Europe Economics was commissioned by the European Securities and Markets Authority (ESMA) to collect data on the costs associated with ESMA's draft technical standards for the Market Abuse Regulation (MAR). The draft technical standard assessed in this report relate to:

- buy-back programmes and stabilisations;
- market soundings;
- detection, prevention, and reporting of suspicious orders and transactions (STORs);
- delays to the disclosure of insider information;
- transactions by persons discharging managerial responsibilities (PDMRs); and
- objective presentation and the disclosure of interests/conflicts of interest in investment recommendations.

We assess the impacts on sell-side firms, buy-side firms, issuers, and trading venues. We summarise our findings for each technical standard in ESMA's impact assessment format below.

1.1 Share buy-backs and stabilisations

Table 1.1: Cost assessment of technical standards on share buy-backs and stabilisations

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	Negligible; largely staff training and potentially IT to receive information on buy-backs and stabilisations.	Not assessed
	Ongoing	Data processing and investigating may be multiplied due to the need to report to each competent authority where buy-backs and stabilisations occur (rather than one competent authority).	Not assessed
Compliance costs	One-off	Costs accrue only to sell-side firms and issuers. One-off costs largely relate to IT systems investment for sell-side firms and some staff training costs.	€4.0m - €5.6m
	Ongoing	Costs accrue only to sell-side firms and are almost exclusively for the ongoing maintenance of IT systems. Despite foreseeing some small one-off costs, issuers did not anticipate any ongoing costs.	€0.3m - €0.5m
Indirect costs		While there is a possibility that the requirement to report to multiple competent authorities could alter capital market interventions, stakeholder feedback and our own analysis indicate that this is quite unlikely.	Not assessed

1.2 Market soundings

Table 1.2: Cost assessment of technical standards on market soundings

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	None / Negligible	Not assessed
	Ongoing	None / Negligible	Not assessed
Compliance costs	One-off	The main impacts fall on DMPs, which can be sell-side firms or issuers, with sell-side firms bearing the bulk of the costs. Sell-side firms' costs will mostly be in IT investment and in developing and maintaining sounding scripts. Sell-side firms and issuers mentioned staff training and additional due diligence prior to making soundings, but these were relatively minor, particularly in view of the IT and script costs. For the remaining stakeholder groups, costs tended to relate to familiarising the business with the regulation and training staff on how to comply with the regulation.	€9.3m - €15.3m
	Ongoing	Annual ongoing costs are highest for sell-side firms and issuers. Ongoing costs relate to maintaining and revising scripts, which would be relevant to issuers as DMPs. Some of these costs could also relate to storing script-related and transmission-related sounding information. Sell-side firms in particular will realise ongoing costs for maintaining IT systems and market sounding scripts, with some fairly minor costs for additional pre-sounding due diligence on information.	€6.4m - €9.3m
Indirect costs		Our research found that many buy-side participants already have misgivings about being sounded and that the lack of a cleansing strategy could exacerbate them. Whilst this could result in lower buy-side participation in pre-transactions soundings and thus lower quality information used to advise in capital markets operations, we note that this is not due to L2 per se, but because the L1 regulation does not provide a clear cleansing strategy. We included it here as it was the key issue raised by respondents in our work on this Standard.	Not assessed

1.3 STORs

Table 1.3: Cost assessment of technical standards on STORs

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	Negligible; some staff training and possibly IT investment.	Not assessed
	Ongoing	None / Negligible	Not assessed
Compliance costs	One-off	Most costs accrue to sell-side firms, with some impact on EAMPs and trading venues. The greatest cost impact comes from investment in IT systems, of which the bulk of the costs are investing in a system to meet the automated surveillance requirement. Increasing reporting to competent authorities and staff training are notable one-off costs. Storage of information will add to compliance costs, with most costs for EAMPs and trading venue arising from this requirement.	€29.7m - €42.2m
	Ongoing	Ongoing costs are driven by maintenance of IT systems, additional investigation of suspicious activities, and additional reporting to competent authorities. These costs arise for sell-side firms, EAMPs, and trading venues, with sell-side firms having the highest costs.	€14.5m - €20.6m
Indirect costs		No anticipated wider effects.	Not assessed

1.4 Disclosure and delays to disclosure of inside information

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	Minor one-off cost of assigning a dedicated point of contact to each issuer and in setting up a template for notification to issuers of delays to disclosure for the purpose of financial stability have been granted.	Not assessed
	Ongoing	Minor costs in clarifying the delays process to issuers and in producing written notifications of whether an issuers' request to delay for the purpose of financial stability has been granted.	Not assessed
Compliance costs	One-off	The most impacted stakeholders are issuers. The key cost drivers are investing in new IT systems and employing external professional services. These compliances costs are not expected to be material relative to firm's operating expenditure.	€43.4m - €86.4m
	Ongoing	Issuers are the most impacted, with the buy-side and trading venues experiencing no ongoing costs. The principal ongoing costs are the conducting of additional internal reporting and the maintenance of IT systems.	€6.8m - €16.5m
Indirect costs		There are mixed views with regard to the impact on the attractiveness of non-regulated markets relative to regulated markets. There is some belief that it could deter SMEs from listing on non-regulated markets, although it is difficult to disentangle the impacts relating to L1 (the disclosure requirement) and L2 (the technical means for disclosure and delays).	Not assessed

1.5 Insider lists

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	Minor, limited to some staff training costs in understanding the format of insider lists and minor IT investments to allow for storage of the additional information contained in insider lists.	Not assessed
	Ongoing	Minor: additional staff time will be needed for processing additional information received from issuers and in merging the insider lists from issuers and their related third parties. These costs will again not be material.	Not assessed
Compliance costs	One-off	One-off costs are primarily incurred by sell-side firms and issuers The key cost driver is due to developing additional IT systems infrastructure or upgrading existing infrastructure. Several stakeholders spoke of this in the context of linking up content in existing HR databases with the insider lists.	€21.0m – 33.5m
	Ongoing	The key determinant of ongoing compliance costs is that of maintaining and reviewing insider lists, given the detailed nature of the information that must be collected on insiders and kept up-to-date.	€25.9m - €35.7m
Indirect costs		The key indirect cost is that the information requirements of the draft technical standards are seen by stakeholders as an excessive invasion of personal privacy, and doubt whether the benefit to investor protection is commensurate.	Not assessed

1.6 Format for PDMR Notifications

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	As with the format of insider lists, we expect very minor, non-material costs to arise through the same channels as those for insider lists.	Not assessed
	Ongoing	There will be only very minor ongoing costs of staff time in processing the additional information contained in PDMR templates/ notifications.	Not assessed
Compliance costs	One-off	The one-off per firm compliance costs are significantly higher for the sell-side than for other stakeholder groups. With the exception of minor costs for understanding the regulation and training reported by trading venues, trading venues and the buy-side anticipate no compliance costs. The key cost driver is the cost of developing additional IT systems infrastructure or upgrading existing infrastructure.	€13.7m - €19.4m
	Ongoing	Ongoing IT maintenance and the maintenance and review of PDMR templates/ notifications are the two main ongoing costs. This is a reflection of the more detailed information requirements for PDMRs, as well as for closely associated persons for whom stakeholders believe it will be particularly difficult and costly to obtain information.	€0.7m - €0.9m
Indirect costs		The key concern is that the informational requirements are excessive and represent an invasion of personal privacy for no material gain. Firms expect that it will be particularly difficult to make PDMRs provide details on closely associated persons.	Not assessed

1.7 Objectivity and conflicts of interest in investment recommendations

	Timing	Qualitative description	Quantitative description
Costs to regulator	One-off	None/negligible	Not assessed
	Ongoing	None/negligible	Not assessed
Compliance costs	One-off	With the exception of some issuers reporting very minor one-off understanding and training costs, the compliance costs fall exclusively on sell-side firms and, therein, should be limited to the larger sell-side firms who are responsible for producing sell-side research. The evidence suggest that the key compliance cost will be the cost of training staff, in order to ensure that the employees producing the investment recommendations conform to the new reporting requirements.	€3.1m - €4.1m
	Ongoing	The ongoing costs are extremely limited and should be exclusively driven by the need for employees of sell-side firms to compile more detail on additional disclosures and for investment recommendations. A large portion of these additional resource costs could relate to the reduction in the significant shareholdings threshold from 5 per cent to 0.05 per cent. Nevertheless, these costs will not materially impact on firms' operating expenditures.	€0.5m - €0.7m
Indirect costs		The evidence of any adverse impact on the timely dissemination of investment recommendations is mixed, although few proposed a knock-on effect on liquidity in some investments. Stakeholders were generally not of the view that the draft technical standards would stimulate more client queries and nor that innovation and the willingness to develop new valuation approaches would be materially impeded.	Not assessed

1.8 Summary of compliance costs by firm

We present below summary tables showing the impact by firm across all of the Technical Standards.

We note, however, that in some places stakeholders had difficulty in separating L2 impacts from L1 impacts. We have tried to note this qualitatively and, where justifiable, attempt to isolate just the L2 impacts. Nonetheless, it is likely that there is some element of L1 cost embedded in these figures. Therefore, these ranges may potentially over-state the true range for the L2 MAR technical standards.

Table 1.4: Per firm one-off compliance costs for all technical standards (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	795.2	1,131.2	117.6	166.3	9.2	12.2
Buy-side	24.7	33.2	3.7	5.0	0.4	0.5
Issuer	123.6	219.3	21.3	37.8	2.0	3.5
Trading	73.2	99.0	11.0	14.8	1.1	1.5

Source: Europe Economics estimates.

Table 1.5: Per firm ongoing compliance costs for all technical standards (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	179.1	278.7	25.9	40.3	2.2	3.3
Buy-side	33.9	45.8	5.1	6.9	0.5	0.7
Issuer	86.9	128.2	15.1	22.3	1.0	1.5
Trading	57.9	78.3	8.7	11.7	0.9	1.2

Source: Europe Economics estimates.

1.9 Summary of total compliance costs by Technical Standard

We present below summary tables showing the impact by Technical Standard. Some of the cost impacts are moderately large: this is essentially driven by the populations sizes affected. As we have seen above, the firm-level costs are generally not substantial. It is important to recall that behavioural effects are driven by these firm-level impacts.

Table 1.6: One-off compliance costs for all technical standards (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Buy backs	2.5	3.5	1.5	2.1	0.0	0.0	**4.0**	**5.6**
Market soundings	5.7	9.5	3.5	5.7	0.1	0.1	**9.3**	**15.3**
STORs	7.4	10.4	3.5	4.9	18.8	26.9	**29.7**	**42.2**
Inside information	16.8	33.0	19.9	40.3	6.7	13.1	**43.4**	**86.4**
Insider lists	8.6	13.6	8.6	14.1	3.8	5.9	**21.0**	**33.5**
PDMR	5.1	7.2	6.5	9.2	2.1	2.9	**13.7**	**19.4**
Conflicts of interest	2.0	2.7	1.1	1.5	0.0	0.0	**3.1**	**4.1**
Total	**48.0**	**79.9**	**44.5**	**77.8**	**31.6**	**49.0**	**124.1**	**206.7**

Source: Europe Economics estimates.

Table 1.7: Annual ongoing compliance costs for all technical standards (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Buy backs	0.2	0.3	0.1	0.2	0.0	0.0	**0.3**	**0.5**
Market soundings	3.6	5.3	2.7	3.9	0.0	0.0	**6.4**	**9.3**
STORs	4.1	5.7	1.7	2.5	8.7	12.4	**14.5**	**20.6**
Inside information	2.7	6.3	3.1	7.7	1.0	2.4	**6.8**	**16.5**
Insider lists	9.2	12.7	11.8	16.2	4.9	6.8	**25.9**	**35.7**
PDMR	0.3	0.4	0.3	0.4	0.1	0.1	**0.7**	**0.9**
Conflicts of interest	0.3	0.4	0.2	0.2	0.0	0.0	**0.5**	**0.7**
Total	20.3	31.2	20.0	31.2	14.7	21.8	55.0	84.2

Source: Europe Economics estimates.

2 Introduction

This report was commissioned by the European Securities and Markets Authority (ESMA) to collect data on the costs associated with ESMA's draft technical standards for the Market Abuse Regulation (MAR), under contract PROC/2014/003. From the terms of reference, the purpose of the research is to:

> "conduct and deliver a study which supports ESMA on its cost-benefit analysis for technical standards in the context of the Market Abuse Regulation (MAR). The aim of the study is to gather and analyse data on the scope and costs of a number of technical standards ESMA has to draft of the context of the MAR."

The remainder of the report is organised as follows:

- Section 3 provides a brief history of regulation on market abuse in Europe and demographic information about the key stakeholder groups affected by the MAR.
- Section 4 presents a qualitative and quantitative compliance cost analysis of ESMA's draft technical standards and also discusses what wider costs might arise in respect of each standard.
- Appendices describe our research methods, sample, and cost modelling approach, and also set out the survey questions and background material provided to stakeholders participating in our fieldwork.

3 Background and Counterfactual

This section is intended to provide context to this report. We begin by discussing what market abuse is and how European authorities have sought to address it and then describes some of the key stakeholder groups affected by regulation on market abuse.

3.1 Background on market abuse and regulation

Market abuse refers to two main activities conducted on and related to financial markets. First, 'insider dealing' occurs when an individual or entity buys or sells financial instruments while in possession of inside information about those instruments. Chapter 2 Article 7 of the final MAR text defines inside information is

> "information of a precise nature, which has not been made public, relating, directly or indirectly to one or more such derivatives or relating directly to the related spot commodity contract, and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments".

Second, 'market manipulation' is changing the price of a security by, for example, disseminating false or misleading information or rumours about that security or by employing a fictitious device or any other form of deception or contrivance, as well as giving, or being likely to give a false or misleading signal about the supply of, demand for, or price of a security or securing a security at a price deemed to be abnormal or artificial.

Market abuse prevents the well-functioning of financial markets by, *inter alia*, distorting information conveyed by price signals, harming trust in financial markets as information asymmetries persist, and, in consequence, allocating capital sub-optimally.

In 2003, the European Commission introduced the Market Abuse Directive (MAD), which aimed to further empower national regulatory authorities to counter and sanction market abuse within their jurisdictions, over and above prior efforts at the national level. Furthermore, the MAD obliged a number of stakeholders to provide transparency through tools such as insider lists, restrictions and reports on manager transactions, and the monitoring and reporting of suspicious transactions.

Requirements of the MAD extended largely to Regulated Markets (RMs), as the bulk of trading in financial securities was done on these platforms in 2003. Trading on other venues, such as Multilateral Trading Facilities (MTFs) or Organised Trading Facilities (OTFs), was less common at the time. In addition, certain instruments that are relatively widely traded and more liquid now were less so in 2003. A series of financial scandals, including the manipulation of certain key financial benchmarks, and the perceived limited powers of regulatory authorities to sanction market abuse highlighted certain weaknesses with the existing framework. In short, the diversity of financial markets and the authorities' ability to regulate them had changed sufficiently to justify updating the MAD, both to keep pace with the evolution of financial markets and strengthen the tools available to regulators to ensure the market is fair and efficient.

This updated framework, the Market Abuse Regulation (MAR), extends the scope of the regulation of market abuse to new trading venues, including MTFs, OTFs, emissions markets, small and medium sized (SME) growth markets, and other trading venues not covered previously under the MAD (indeed, some of these concepts were not extant at the time of its conception), as well as to new financial instruments and contracts.[1] What is more, the MAR introduces enhanced means to detect market abuse and includes tougher sanctions for those who engage in market abuse, such as requiring automated surveillance of market activity. In order to allow smaller firms to access public capital markets while also ensuring that SME growth markets are subject to market abuse prohibitions, the MAR has in place a number of provisions to ease the administrative burden on SME issuers.

We note that although the MAR itself covers a variety of topics, the aim of this report is to assess topics relating to ESMA's remit to develop technical standards for the MAR. To this end, we do not review the MAR itself in detail. Instead, we focus our more detailed discussion of the MAR on a selection of ESMA's technical standards, which are discussed in detail in Section 4. The focus of this discussion is not the effects arising from the MAR itself, but rather those relating to ESMA's technical standards.

3.2 Key stakeholders

In this section we give some descriptive statistics on the key stakeholder groups involved. The types of organisation operating in securities markets that we expected to be affected were:

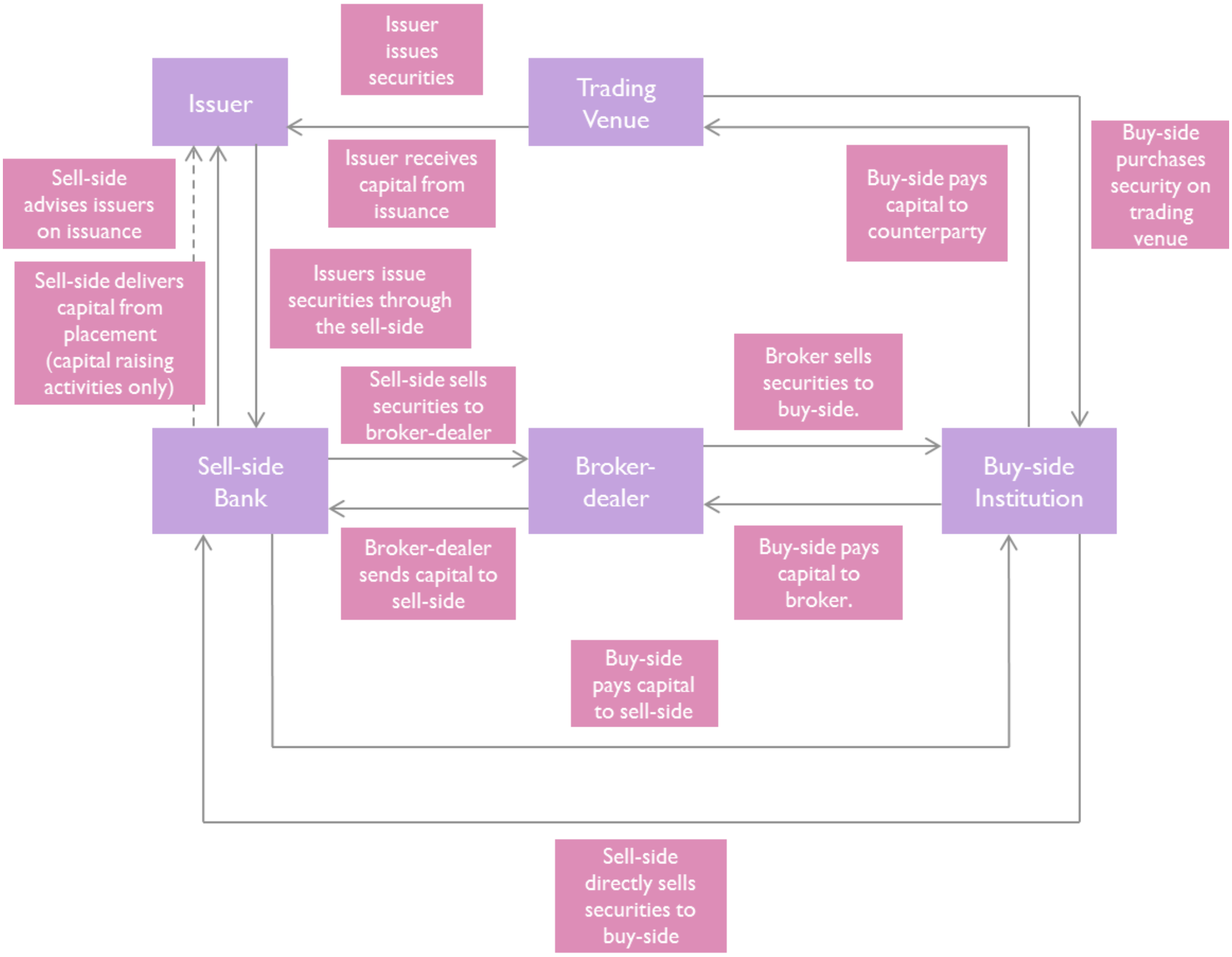
- Trading venues.
- Issuers.
- Sell-side firms.
- Non-bank brokers and dealers.
- Buy-side firms (i.e. institutional investors).

Given that one of the overall objectives of the MAR is to improve investor protection, a further key stakeholder group to consider would be retail investors. However, in practice, given the nature of the Technical Standards it is unlikely there are any directly measurable cost implications on retail investors. Instead, by analysing, and quantifying where possible, the compliance costs and wider impacts for the organisations in our sample, the potential knock-on effects for retail investors (i.e. whether and to what extent costs might be passed on to this group) can also be considered. Another important set of stakeholders to consider are the competent authorities, as the organisations with regulatory oversight and enforcement of their national securities market. However we have only considered the impacts on this group in qualitative terms.

Figure 3.1 presents a stylised, simplified model of the kind of securities markets covered by ESMA's technical standards for the MAR. Issuers seeking to raise capital on markets issue securities, either directly on trading venues (often advised by sell-side banks) or indirectly by selling securities through the sell-side (e.g. a "bought deal"). For the latter, sell-side banks sell the securities through a broker-dealer or place the securities directly to the buy-side. In each case, capital flows from the right-hand side of the figure to the left-hand side, while securities flow from the left-hand side to the right-hand side. In principle, national competent authorities will watch each arrow in the model, as exploitation of inside information or market manipulation can occur or be detected in each point in the capital / securities flow.

[1] See MAR Article 2 on the scope of the Regulation for details.

Figure 3.1: Simplified model of securities markets



Source: Europe Economics.

3.2.1 Trading venues

The final MAR text specifies that any financial instrument traded on a regulated market, an MTF or an OTF is subject to market abuse regulation. We use the MiFID II definitions of each type of trading venue. Each is now considered in turn.

Regulated Markets

Regulated Markets are markets listed by the Competent Authority of every country, which are submitted to ESMA and other Competent Authorities on an annual basis. The population of Regulated Markets is assessed using the MiFID database, as shown below.

Table 3.1: RMs by country

Country	RMs
Austria	2
Belgium	2
Bulgaria	1
Croatia	1
Cyprus	1
Czech Republic	3
Denmark	2
Estonia	1
Finland	1
France	4
Germany	15
Greece	3
Hungary	1
Ireland	1
Italy	9
Latvia	1
Lithuania	1
Luxembourg	1
Malta	2
Netherlands	5
Poland	6
Portugal	3
Romania	4
Slovakia	1
Slovenia	1
Spain	12
Sweden	2
United Kingdom	10
Grand Total	96

Source: MiFID database; Europe Economics analysis. The MiFID database also includes an RM in Iceland and four in Norway.

There are 96 Regulated Markets across the EU28 (see Table 3.2). Most countries have only a small number. Germany and the United Kingdom have a higher than average number of regulated markets, with 15 and 10 respectively. Spain (12) and Italy (9) also have a relatively high number.

Multilateral trading facilities

In total, there are 146 MTFs in the EU, according to the MiFID database maintained by ESMA, as shown in Table 3.2.[2] Again, most countries have only a small number of MTFs, with 11 countries having only one. The UK and Germany are the only two countries with more than ten MTFs, with a total of 74 and 13 MTFs respectively — indeed, the UK is home to other half of the EU's population of MTFs. Italy and Belgium also have a relatively high number, with nine and eight in these two Member States respectively.

[2] See: http://mifiddatabase.esma.europa.eu/.

Table 3.2: MTFs by country

Country	MTFs
Austria	1
Belgium	8
Bulgaria	0
Croatia	1
Cyprus	1
Czech Republic	2
Denmark	3
Estonia	1
Finland	1
France	6
Germany	13
Greece	1
Hungary	1
Ireland	3
Italy	9
Latvia	1
Lithuania	1
Luxembourg	1
Malta	0
Netherlands	3
Poland	3
Portugal	3
Romania	2
Slovakia	0
Slovenia	0
Spain	4
Sweden	3
United Kingdom	74
Grand Total	146

Source: MiFID database. The MiFID database also includes an MTF in Iceland and three in Norway

SME Growth Markets

MiFID II introduces the concept of an SME Growth Market. By definition an SME Growth Market will be an MTF and so these markets will constitute a subset of the MTFs in the EU. However, there are no SME Growth Markets *per se* and hence no definitive listing of them. Using the MiFID database (see Table 3.2) as our starting point we identified about 40 potential SME Growth Markets among the existing MTFs in the EU. Five countries have no candidate SME Growth Markets, with a further 14 having a sole SME Growth Market. Collectively, Germany and the United Kingdom account for eight and five of the SME Growth Markets, respectively.

Data from some of these candidate markets are, in some instances, very sparse and some of these MTFs may be little more than placeholders awaiting future development. Therefore, we focus on the more developed SME Growth Market candidates. Data are sourced from a combination of Bloomberg and the websites of the trading venues themselves. A key test in identifying SME Growth Markets is that the median market capitalisation is less than €200 million for each of the last three years. Table 3.3 below reports exclusively 2013 data, but prior review of 2013 data in conjunction with 2011 and 2012 data showed that all of these SME Growth Market candidates — those for whom data are readily available —

are well within this proposed threshold. The only exception is Prague's START market which, although targeted at smaller growing businesses, only had one listed member as of 31st December 2013, which was a large brewer with a primary listing on the London Stock Exchange.

Table 3.3: Analysis of main SME Growth Market candidates

Trading Venue	Issuers	Total Market Capitalisation (€bn) (31/12/2013)	Median Market Capitalisation (€m)	Total trading turnover 2013 (€m)
NYSE Alternext (FR, NL, BE, PT)	169	7.8	21.0	14,362
Cyprus ECM	10	0.6	39.5	1
Prague START (CZ)	1	0.7	698.8	n/a
DB Entry Standard (DE)	174	58.4	20.3	8,340
First North (SE, DK, FI — and IS)	135	4.0	10.3	313
MAB (ES)	23	1.2	19.3	n/a
ISDX (UK)	102	2.6	1.9	n/a
AIM (UK)	1,062	90.8	24.8	38,007
ATHEX (EL)	14	0.1	8.2	1
ISE ESM (IE)	25	63.3	91.0	n/a
AIM Italia (IT)	36	1.1	19.3	160
Warsaw New Connect (PL)	445	2.7	1.9	225
Total	**2,196**	**233.4**		**61,679**

Source: Europe Economics analysis based on venues' own publicly available data.

There are also several markets for which little information is readily available other than the number of issuers. In particular, we note that Aktietorget (Sweden), ISDX Growth (UK) and GXG First Quote (Denmark) have between them about 200 issuers. On the basis of this and the detailed analysis in the above table we consider an estimate of about 2,500 issuers on SME Growth Markets to be reasonable.

Organised trading facilities

OTFs are a new category of trading venue under MiFID II/MiFIR, therefore, a precise quantification of this population is somewhat difficult. For calculating compliance costs, we estimate that there are around 25 impacted venues that would be classified as OTFs.

Emissions venues

There are four product types traded on emissions venues:

- European Union Allowances (EUAs).
- Emissions Reduction Units (ERUs).
- Certified Emissions Reductions (CERs).
- European Union Aviation Allowances (EUAAs).

EUAs are the basic emission allowances which allow firms to pollute one lot (1,000 tonnes) of CO_2. To date there have been three phases of EUAs, although Phase I EUAs were discontinued with the introduction of Phase II EUAs. Therefore, only Phase II and Phase III EUAs are currently traded. ERUs are emissions units issued under a Joint Implementation project, while CERs are those issued under the Clean Development Mechanism. EUAAs are special emission allowances which are exclusively for use by airline companies for compliance purposes. There are both spot and derivatives (futures) markets for the products discussed above.

There are four exchanges for emissions market products, with ECX constituting over 90 per cent of the market.

Table 3.4: Market share of emissions trading venues in Europe

Trading Venue	ECX/ICE	NASDAQ OMX	EEX	CME
Market share* (June 2014)	92.9%	0.1%	6.5%	0.5%

Note: *Primary and Secondary Market, including primary auctions.
Source: ICE.

Table 3.4 shows that ECX/ICE and EEX collectively constitute over 99 per cent of the market. The number of emission market participants on these two key emissions trading venues is shown in Table 3.3 below.

Table 3.3: Number of emissions market participants on ECX/ICE and EEX trading venues

	Spot	Derivatives	Spot and/or Derivatives	Future
ECX/ICE	-	-	-	130*
EEX	141	154	174**	-

* Of the 130 emissions market futures participants, 62 are trade participants who cannot trade on behalf of clients, clear clients' business or do give ups, and 68 are general participants who can carry out such functions either for their own business, or for clients' business.
** The number of participants in the spot and derivatives is substantially less than the sum of the number of participants in spot and the number of participants in derivatives because several firms operate in both markets.

Given the substantial degree of overlap in organisations participating on these two trading venues, and given that ECX/ICE constitutes over 90 per cent of the total market for emissions trading, for a market sizing purpose it is estimated that at least 180 organisations are active traders in this market.

3.2.2 Issuers

Drawing again on the MiFID database, there were around 5,954 securities trading on regulated markets. On the basis of this data, we estimate that around 5,689 are unique firms,[3] with some firms having multiple listings due to different classes of listed shares. In addition, as noted above, we believe there are around 2,500 equity issuers on SME Growth Markets.

Data from the Federation of European Securities Exchanges (FESE)[4] contain information on all major EU securities exchanges, with the exception of those exchanges that are part of the London Stock Exchange Group, i.e. the London Stock Exchange and Borsa Italiana. These data indicate that there are 7,782 companies covered by FESE member exchanges. There are 2,436 companies listed on the London Stock Exchange as of 31st October 2014,[5] and a further 340 companies listed on the Borsa Italiana as of the same date.[6] Together this implies a total number of issuers to 10,558 companies. (Bond issues are difficult to tie back to issuer numbers, as issuers will tend to issue multiple tranches of bonds with different currencies and maturities for example. We have assumed that the bond issuer population overlaps entirely with that for equity issuers).

On this basis, there is a large discrepancy between the FESE estimates and the estimates produced using the MiFID database. The discrepancy is largely driven by the number of companies identified in the FESE data as being listed on Spanish markets. We have preferred the MiFID database-derived numbers, which we have supplemented with our estimate of the number of firms with primary issuance on an SME Growth Market (which we take as a proxy for those firms with instruments exclusively traded on an MTF). We are

3 This figure includes listed subsidiaries of listed parent companies.
4 FESE statistics database, available at: http://www.fese.eu/en/?inc=page&id=10.
5 London Stock Exchange Companies and Issuers, available at: http://www.londonstockexchange.com/statistics/companies-and-issuers/companies-and-issuers.htm.
6 Borsa Italiana Monthly Update, October 2014, available at: http://www.borsaitaliana.it/borsaitaliana/statistiche/sintesi-mensili/2014/sintesimensili201410.en_pdf.htm.

aware that some securities issued in non-EU jurisdictions are traded on EU markets without the explicit consent of the issuer. These have been excluded from our population estimates.

3.2.3 Sell-side firms and non-bank brokers and dealers

In this context, sell-side firms advise companies on issuance in public markets and act as intermediaries that place securities with investors in private dealings.

A previous study on the costs of changing the MAD done on behalf of the European Commission used information on credit institutions and other deposit-taking corporations as their measure of the size of the sell-side firm market.[7] This would imply over 7,000 firms in the sell-side community.[8] However, we do not believe this necessarily represents a reliable estimate of the size of the market for our purposes, since not all of these credit institutions and other deposit-taking corporations are involved in the sort of activities covered by the MAR, and investment firms which are not credit institutions may undertake relevant activities.

Based on a survey conducted for Europe Economics in relation to work for the European Commission on the MiFID Framework Directive in 2009-2010, national competent authorities indicated that only around 44 per cent of credit institutions across the EU were involved in any investment services. Of these, between 60 and 90 per cent were involved in activities covered by ESMA's technical standards (e.g. any of reception and transmission of orders, execution of orders on behalf of clients, under writing and placing, etc.).[9] From the same survey we also have data on investment firms. Obviously all investment firms are authorised for at least one investment service, with 88 per cent authorised at the time of that survey for the receipt and transmission of orders, and 18 per cent for underwriting and placing.

Table 3.5 combines information from that original survey, and updated data from the European Banking Authority (the EBA) on the total number of authorised investment firms and credit institutions. The latest available data are for the end of 2012. We consider the categories of greatest relevance are 'receipt and transmission of orders', and 'underwriting and placing', which we use to estimate the population figures below.

Table 3.5: Number of credit institutions and investment firms authorised for selected investment services, 2012

	Credit Institutions	Investment Firms
Underwriting and placing	1,275	700
Receipt and transmission of orders	1,900	3,510

Source: Survey of national competent authorities conducted by CESR on behalf of Europe Economics (2010), EBA data on number of Investment Firms and Credit Institutions (2012).

This gives a consolidated number of firms authorised for the receipt and transmission of orders of 5,410. About 1,975 firms are authorised to undertake underwriting and placing activities.

We emphasise that these estimates of the population of sell-side banks and non-bank brokers and dealers impacted by the MAR is of those authorised. In many Member States the marginal cost of authorisation for a particular investment service is quite low — in other words the number of authorised firms may well exceed the number of active firms by a substantial margin.

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7 EIM (2011) "Study 1: effects of possible changes to the Market Abuse Directive: impact on administrative burdens of enterprises in the EU", p22.

8 According to ECB data on MFIs for August 2014.

9 These are MiFID investment services. Although carrying out MiFID-related services does not necessarily imply that one is covered by MAR, we believe it is unproblematic to use these designations as a proxy for market sizing as an entity performing these particular services would almost certainly be covered by the MAR.

3.2.4 Buy-side firms

According to the European Fund Management Association, there were approximately 3,200 asset management companies in 2012.[10] At the close of 2013, total assets under management in these firms was around €16.8 trillion.[11]

Table 3.6: Number of asset managers in the EU by Member State

Country	2011	2012
Austria	29	29
Belgium	87	87
Bulgaria	33	32
Czech Republic	21	21
Denmark	16	16
Finland	35	35
France	599	604
Germany	293	296
Greece	60	56
Hungary	35	35
Ireland	431	431
Italy	283	276
Luxembourg	361	351
Netherlands	196	196
Poland	36	36
Portugal	81	81
Romania	21	21
Slovakia	13	13
Slovenia	11	11
Spain	115	107
Sweden	78	74
United Kingdom	191	194
Total	3,025	3,002

Source: EFAMA.

As of 2012, EFAMA data show that France have the most asset managers in Europe with 604. This is followed by 431 in Ireland, 351 in Luxembourg, and 296 in Germany. EFAMA does not have member associations in all of the EU's countries. To make some allowance for this we adopt 3,200 as our pan-EU estimate.

3.2.5 Competent authorities

Under ESMA's proposed technical standards, the increased reporting requirements for various organisations operating in securities markets should mean that competent authorities are equipped with new, more detailed, and/or more timely information with which to address market abuse in their jurisdictions. In this way, ESMA's technical standards, in addition to the Level 1 standards set out in MAR, will help to enhance the ability of competent authorities to prevent, detect and sanction market abuse. However, the increased reporting requirements to competent authorities are likely to increase the costs to

[10] EFAMA (2014) "Asset management in Europe", p30.
[11] EFAMA (2014) "Asset management in Europe", p2.

these stakeholders, such as by increasing data processing costs. We note, however, that much of this impact will arise from the MAR L1 standards rather than ESMA's proposed technical standards.

Each Member State has a competent authority (and in some cases, e.g. Germany, multiple authorities) that is responsible for monitoring for, detecting, and sanctioning market abuse. Data on the number of supervisory staff with specific reference to the detection of market abuse are not available.

3.3 Specifying the counterfactual

The counterfactual in this case is the evolution of financial markets with the MAR but without ESMA's technical standards. The impacts of the MAR are the "Level 1" ("L1") impacts, while the incremental impacts of ESMA's technical standards are the "Level 2" ("L2") impacts. Thus, the impacts this report assesses are quite granular and in addition to the impacts that already arise from the MAR itself.

In terms of market evolution, we assume that markets newly-covered under the MAR, such as MTFs (including SME growth markets) and emissions markets, will need to comply with various MAR provisions. For example, Article 18 of the MAR specifies the creation of insider lists to include all individuals directly employed by issuers, or engaged in an indirect role, such as accountancy or advisory services. This requirement is an L1 impact and would occur in the absence of any of ESMA's technical standards. However, the specificities with regard to what information should be disclosed in insider lists and the format and delivery of these lists are technical standards outlined by ESMA and will have impacts attributable to that standard.

Our analysis focuses, then, on the incremental impacts that stakeholders have identified that arise due to ESMA's technical standards for complying with the MAR. Subsequent sections focus their discussions on ESMA's technical standards, what stakeholders have said in relation to those standards, and the costs and wider effects that emerge from those standards.

4 Mechanisms of Effect and Cost Analysis

The first step in assessing the costs of ESMA's draft technical standards for implementing the MAR is to map out the economic logic connecting the technical standards to costs and other market impacts. We call such a map the "mechanisms of effect".

At a high level, the draft technical standards we assess relate to:

- buy-back programmes and stabilisations;
- market soundings;
- detection, prevention, and reporting of suspicious orders and transactions;
- delays to the disclosure of insider information;
- transactions by persons discharging managerial responsibilities; and
- objective presentation and the disclosure of interests/conflicts of interest in investment recommendations.

For each of these categories of technical standards, ESMA has defined the aspects of the technical standards that we investigate. In some instances (e.g. buy-backs and stabilisations) this covers the vast majority of the technical standards in the category. For other categories, ESMA has requested that we assess the costs of particular aspects of the technical standards (e.g. analysing costs associated only with the format of the insider list for transactions by persons discharging managerial responsibilities).

We discuss each technical standard category below. Our primary basis for this discussion is ESMA's July 2014 Consultation Paper on the draft technical standards.[12] Within each technical standard category, we review the technical standards in the area with special emphasis on the technical standards within the scope of our research, outline the mechanisms of effect connecting the technical standards to economic impacts, and give a qualitative discussion of the costs and other impacts that may arise due to the technical standards. We then present the quantitative compliance costs which have been estimated using the data obtained in the stakeholder engagement. Costs are presented on a per firm and aggregate cost basis for each of the stakeholder categories identified in Section 3.2 (except for competent authorities), and in doing so we explain how we reached an appropriate estimate of the affected population for each technical standard.

4.1 Buy-back programmes and stabilisations

Issuers purchasing their own shares can be market abusive, e.g. an investor or institution purchasing a security with the aim of supporting the security's price. However, there are legitimate reasons for stabilising a financial instrument or for an issuer to trade in its own shares, justifying that such trades would be exempt from the insider trading and market manipulation prohibitions set out in other areas of the MAR,[13] providing that certain conditions are met (the "safe harbour principle"). ESMA has specified in the technical standards specific conditions that must be satisfied in order to benefit from the safe harbour principle, which we discuss below.

[12] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation".
[13] This was also the case in Article 8 of the Market Abuse Directive (MAD).

4.1.1 Technical standards

Buy-back programmes

For a buy-back programme to benefit from the safe harbour principle, MAR requires that it must "have as its sole purpose:

- "to reduce the capital of an issue; or
- to meet the obligations arising from debt financial instruments that are exchangeable into equity instruments; or
- to meet obligations arising from share option programmes, or other allocations of shares, to employees or to members of the administrative, management, or supervisory bodies of the issuer or associate company."[14]

Where a buy-back programme does have one of the above as its sole purpose, the buy-back programme can benefit from the safe harbour principle where:

- The full details of the programme are publicly disclosed prior to the start of trading — ESMA has defined the relevant details to be disclosed in Article 3(1) of the draft technical standards.[15]
- The buy-back transactions are reported to the Competent Authority and publicly disclosed.[16]

For general public disclosure, ESMA requires that data are published via the website of the issuer conducting the buy-back programme and disseminated through appropriate disclosure channels. For shares trading on Regulated Markets, current practices — that is, those established through the Transparency Directive — for dissemination and storage are sufficient. In other words, there should be no change with respect to current market practices. For other issuers not covered under the Transparency Directive, i.e. MTF only issuers, they will need to disclose the information via the mechanisms and channels set out in that Directive. Aggregated daily repurchase volumes and volume-weighted average purchase price per venue will be displayed on the issuer's website no later than the end of the seventh market session[17] following the date of the execution of the reported transactions.

For disclosure to Competent Authorities, detailed transaction information will be provided for every transaction, rather than the aggregated information provided to the general public, and no later than the end of the seventh market session. The "investment firms concerned" will refer to the investment firm that is conducting the buy-back on behalf of the issuer, rather than the counterparty selling the securities. Issuers will need to report information on buy-back activity to the relevant Competent Authority for each regulated market or MTF on which the buy-back is conducted.

The price limit and volume conditions defined in the ESMA TS are complied with

Shares cannot be repurchased at a price higher than the highest previous independent trade or the highest existing bid price.[18] These price limitations apply for the venue on which the buy-back will occur. Share buy-backs will enjoy safe harbour status only on trading venues covered by the MAR and not in OTC markets.

If an issuer's shares are traded continuously throughout the day, then buy-backs during a share auction would not fall under the safe harbour principle. If, however, the shares trade on an auction-only market

[14] Article 5(2) of: Council Regulation (EC) 596/2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC [2014] L173/1 (referred to throughout as "the MAR").

[15] These are the fields to be reported under the current regime.

[16] Information on the content of these disclosures is specified in Article 5(3) of MAR.

[17] The rule on timing for reporting buy-backs is the same as the requirement under the MAD.

[18] This is the same as under the current regime.

(i.e. not continuously), then buy-backs executed during an auction benefit from safe harbour, but such orders cannot be placed during the last instant before the end of an auction.

Buy-backs cannot exceed 25 per cent of the daily average volume of shares traded over a period of reference and there is no longer allowance for exceeding this 25 per cent threshold in a situation of "extreme low liquidity" as under the current MAD regime. Daily averages will be calculated for the venues in which the share buy-backs will be conducted.

The transactions executed that do not fall under a restriction defined in the TS

An issuer that is conducting a share buy-back cannot sell shares during the buy-back programme unless the programme is time scheduled, lead/managed independently by an investment firm / credit institution, or, in the case of buy-backs by investment firms / credit institutions, an appropriate "Chinese Wall" is in place between those selling shares and those executing the buy-back programme. For these restrictions and exemptions for own-trading in shares, ESMA reuses the restrictions (and the exemptions to them) currently in place under MAD.

Stabilisation measures

Stabilisations involve the purchase of a security with the aim of supporting the security's price. According to MAR:

> "stabilisation" means a purchase or offer to purchase securities, or a transaction in associated instruments equivalent thereto, which is undertaken by a credit institution or an investment firm in the context of a significant distribution of such relevant securities exclusively for supporting the market price of those securities for a predetermined period of time, due to a selling pressure in such securities. The term "significant distribution" is further defined in Article 3(2)(c) of MAR as an initial or secondary offer of securities that is distinct from ordinary trading both in terms of the amount in value of the securities to be offered and the selling method to be employed.[19]

Unlike buy-backs, instruments other than shares, such as convertible and non-convertible fixed income securities, can be purchased under stabilisations.

In order to benefit from the safe harbour principle, stabilisation measures and transactions must comply with certain conditions specified in the ESMA technical standards that are essentially similar to those in place under the current regime.

There are different timing restrictions for different classes of securities. For newly-issued shares and securities equivalent to shares, stabilisations may not last longer than 30 days after the shares began trading on the relevant market or the final opening price has been disclosed (for Member States that permit trading in shares before formal issuance). For secondary offerings, stabilisations should begin on the date of disclosure of the final price and may not last longer than 30 days following the allotment date.

For non-convertible and convertible fixed income instruments, stabilisations should begin when the terms of the security are publicly disclosed and end either 30 calendar days after the issuer receives the proceeds of the issuance or 60 calendar days after the allotment of the securities, whichever is shorter.

For securities covered by the Prospectus Directive, ESMA considers the requirements imposed by that Directive sufficient to ensure adequate disclosure of stabilisation activity to market participants. For securities not covered by that Directive, ESMA will require the beginning and end of the stabilisation period to be disclosed to market participants as well as the fact that stabilisation purchases may support the market price during this period. Furthermore, the identity of the entity undertaking that stabilisation on

[19] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p12.

behalf of the issuer — known as the "stabilisation manager" — must also be disclosed, as well as any overallotment facility. This disclosure is under the responsibility of one person appointed by the issuer, offeror and the stabilisation manager among themselves.

Within a week after the stabilisation period has ended, the stabilisation manager must disclose whether stabilisation purchases have taken place, the start and ending date for the period over which the purchases had taken place, and the price range for the purchases.

As with buy-backs, stabilisation disclosures must be reported to each relevant Competent Authority for the markets on which the stabilisation purchases are made and must be disclosed no later than seven market sessions after the date of the transaction in question.

The above reporting obligations must be fulfilled by the stabilisation manager, rather than the issuer. If a consortium is managing the stabilisation activities, then one consortium member should act as a central contact point for transparency-related functions.

Shares cannot be purchased above the prevailing market offer price and fixed income securities cannot be purchased above the market price of those securities at the time of public disclosure of the terms for the new issuance.

Where an overallotment facility exists under a "Greenshoe option" in the underwriting agreement, securities purchased under this facility cannot represent more than 15 per cent of the original offer volume. If there is overallotment not covered by the "Greenshoe option", the overallotment cannot represent more than 5 per cent of the original offer volume.

Transactions benefitting from safe harbour status as stabilisation transactions can only be purchases, rather than sales, since purchases are the only transactions that would support the share price. Therefore "refreshing the greenshoe" activities are excluded from the stabilisation "safe harbour". Additionally, block trades do not enjoy safe harbour status.

4.1.2 Mechanisms of effect

Figure 4.1: Mechanism of effect diagram for buy-backs

Source: Europe Economics.

Figure 4.2: Mechanism of effect diagram for stabilisations

Source: Europe Economics.

4.1.3 Compliance costs and other impacts

Compliance cost impacts

The main cost drivers stemming from these technical standards are report-based and operations-based. From a reporting perspective, one-off and ongoing compliance costs could arise in respect of IT investment, staff training, additional headcount, and reporting requirements.

The bulk of the costs are likely to be borne by issuers and investment firms working on behalf of issuers in managing a buy-back programme or conducting stabilisation activities as part of an underwriting agreement.

Current staff will need to be trained on the requirements for buy-backs and stabilisations. Training is likely to affect a number of different staff categories, such as those close to the compliance function (e.g. compliance staff) as well as those not directly related to the compliance function (e.g. sales and trading at a sell-side financial institution or the treasury staff at an issuer).

Issuers

For issuers, staff working in the compliance function will have to become familiar with new regulatory requirements and set up internal procedures to ensure that various reporting and operational requirements will be satisfied by the issuer. In this case, some of these costs would relate to L1, but other aspects would be attributable to MAR's L2 measures. Therefore, one-off costs will relate to the time required to become familiar with requirements for buy-backs and stabilisations (e.g. the need to post aggregated information on websites but submit disaggregated information to competent authorities; price conditions and volume limitations for buy-backs and stabilisations, etc.) and redesigning internal procedures to ensure compliance. Ongoing costs will relate to the continual monitoring of reports disseminated and securities purchased in buy-backs and stabilisations. To the extent that additional staff would need to be hired to support an issuer's compliance operations, this would be an ongoing cost.

Issuers will also be required to invest in IT systems to log and maintain details on transactions to the general public and competent authorities. Several respondents to ESMA's November 2013 Discussion Paper on draft technical standards noted that costs, including IT investment, of reporting detailed transaction information to the general public would be burdensome. While issuers currently trading on regulated markets already have to keep and report disaggregated transaction information to competent authorities, issuers on newly-covered markets will be required to keep and report this information for the first time.

Another potential class of costs would be reporting costs. Respondents to ESMA's November 2013 Discussion Paper on draft technical standards overwhelmingly favoured reporting information on buy-backs and stabilisations to a single competent authority,[20] although not all participants proposed the same method for determining which competent authority that would be. The principal justification respondents offered for this is that it would minimise costs and other administrative burdens associated with reporting. By contrast, ESMA has proposed that details are reported to the relevant competent authority for the venues on which buy-backs take place. This could multiply a range of operational costs, including the need to monitor different markets with an aim to disaggregating purchases by market and keeping separate reports for different markets. Furthermore, reporting costs will increase as issuers will need to report to multiple competent authorities, which will involve pre-reporting and post-reporting internal procedures to ensure compliance apart from the actual reporting itself. The reporting costs themselves will be ongoing; any one-off costs would likely fall under other categories, such as IT investment or staff training.

We note, however, that there are likely to be some cost synergies associated with reporting to multiple competent authorities. That is, reporting to, say, three competent authorities will not necessarily imply that costs associated with reporting will be three-fold higher. Common costs of reporting can be spread across the compliance function such that the marginal cost of reporting to an additional competent authority falls as the number of competent authorities to whom the issuer reports increases. Nonetheless, it is likely that the requirement to report to multiple competent authorities will increase costs relative to reporting to a single authority.

Although it is possible that the requirement to report to several competent authorities will itself noticeably increase operating costs, we did not find much evidence to indicate that it was a significant cost driver. Sell-side firms and issuers contended this was a relatively minor concern. Sell-side firms said that they would tell their clients about potentially higher reporting costs due to the need to report to multiple competent authorities, but they typically believed that this would have a very limited impact on issuers' operations and the decision about when and where to conduct share buy-backs and stabilisations.

Sell-side institutions

As with issuers, sell-side institutions will face both operational costs and reporting costs. Reporting requirements under buy-back programmes fall on the issuers, but for stabilisations the institution or institutions responsible for conducting the stabilisation programme are required to report the relevant information to the general public and to competent authorities. Many of the key cost drivers for reporting buy-back programmes also hold for reporting stabilisations. For instance, stabilisation managers are

[20] Of the 25 respondents that offered a view, all favoured a single competent authority.

required to report details of the stabilisation purchases to each relevant competent authority rather than a single competent authority. Thus, many of the broad categories of costs will be similar.

Staff training costs will be required to familiarise existing staff with obligations under the MAR and in particular ESMA's technical standards. This will include staff in the compliance function as well as various front office staff. In particular, staff that underwrite equity or fixed income offerings will need to be conscious of MAR requirements regulating the disclosure and transaction conditions surrounding stabilisations. Additional staff may also be required, especially if the sell-side institution has a number of clients in markets newly-regulated under the MAR, such as SME growth markets.

Buy side

Our ex-ante assessment of standards relating to buy-back programmes and stabilisations suggested that buy-side firms are unlikely to incur further costs This impression has been corroborated by the fact that none of the buy-side stakeholders we spoke to indicated that they would incur costs as buy-side operators (although they might as issuers).

Trading venues

Trading venues are unlikely to incur costs from the L2 standards on buy-backs and stabilisations. Indeed, no trading venue stakeholders reported any additional compliance costs arising from the standards.

Competent authorities

The main cost to competent authorities will be in receiving information from issuers and sell-side institutions on buy-back programmes and stabilisations, respectively. Some competent authorities may have had little to no experience in processing the sort of information that ESMA requires to be reported, particularly in such a disaggregated and granular format. This, however, is specified at L1 and reporting content is very similar to that existing under the MAD. On the other hand, competent authorities in larger markets may deal with this sort of information and monitoring the market regularly. Thus, there is reason to expect *ex-ante* that the cost profile may differ among competent authorities.

Like issuers and sell-side institutions, it is likely that competent authorities will have to train staff on the requirements of the MAR. In particular, staff will need to know the fields of information to expect from market participants when receiving information on buy-backs and stabilisations as well as the trading conditions that must be met to enjoy safe harbour status. These training costs will likely be one-off costs. Ongoing costs will arise due to the need to monitor the market for market abuse in buy-backs or stabilisations. Although these costs largely arise from the L1 text, the need to report to multiple competent authorities, proposed in the L2 standards, could multiply the number of authorities monitoring buy-backs or stabilisations by the same firm. Furthermore, certain conditions laid out at the L2 level, such as the requirements for benefiting from safe harbour status, will need to be verified by authorities, which could further increase operating costs.

IT systems investment may be needed to process the information on buy-backs and stabilisations. Since the information will be submitted in machine readable format, it is probable that competent authorities will want to design a system that can read, catalogue, and store information submitted by market participants in a harmonised format. Furthermore, competent authorities will likely require that the system is easily searchable. Again, such costs may be minimal for competent authorities in high-activity countries, but could be considerable for competent authorities that have to date had relatively little interaction with market participants in this way.

Quantitative compliance cost estimates

Of the total population estimates presented in Section 0 and Section 3.2.3, only a part will be impacted by this set of technical standards.

In order to estimate those sell-side firms involved in issuance (and thus stabilisations) or managing buy-back programmes for issuers we used information from the Thomson Reuters equity and debt issuance league tables. Based on these we estimate that there are 24 sell-side banks that we would characterise as large, pan-EU players and 89 that we would characterise as medium (regional or national players) in Europe. We do not anticipate that small sell-side institutions would engage in stabilisations or managing buy-back programmes.

For issuers, we proxy the affected population by combining information on issuers engaging stabilisation purchases with the number of firms that IPO in Europe and issuers that conduct share buy-backs. Information on IPOs come from PwC's IPO Watch Europe Survey[21] and information on share buy-backs come from Bloomberg. We estimate that, in total, around 550 engage in buy-backs or stabilisations in Europe per year, of which approximately 100 are large issuers and 450 are medium-sized issuers.

Issuers reported staff training costs and costs associated with understanding the new regulatory requirements and the impacts on their operations. Compliance costs for issuers are less than a tenth of the compliance costs for sell-side firms on a per firm basis. However, the aggregate compliance costs for issuers are between a quarter and a third of that for sell-side firms, as the population of affected issuers is higher. Issuers did not report any significant staff training costs or new IT costs. From this, we infer that the bulk of the record keeping and reporting costs are likely to fall on issuers' advisers, the sell-side firms.

Table 4.1: Per firm one-off compliance costs for technical standards on buy-backs and stabilisations (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	80.4	114.7	12.1	17.2	1.2	1.7
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	5.6	7.6	1.0	1.3	0.1	0.1
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

Table 4.2: Per firm ongoing compliance costs for technical standards on buy-backs and stabilisations (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	8.9	13.3	1.3	2.0	0.1	0.2
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.0	0.0	0.0	0.0	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

We are not able to quantify the compliance costs for buy-backs separately to those for stabilisations. That said, we believe that the majority of costs for the sell-side would be attributable to the technical standards concerning stabilisation, given the role of sell-side firms in stabilising securities. The costs accruing to issuers would relate exclusively to the technical standards concerning buy-backs.

Table 4.3 presents one-off compliance cost estimates relating to technical standards on buy-backs and stabilisations above. As noted above, the impacted population is issuers and sell-side firms that advise and conduct buy-backs or stabilisations on issuers' behalf. The bulk of the costs fall on sell-side firms. Of this, most of the cost is staff training on new requirements and IT investment to ensure that programmes comply with the technical standards. However, we note that stakeholders were not always able to

[21] PwC (2014) "IPO watch Europe Q4 2014".

differentiate between the L1 and L2 costs to a great degree. Therefore, these estimates are likely to be higher than the true, L2-only impacts.

Table 4.3: One-off compliance costs for technical standards on buy-backs and stabilisations (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	1.9	2.8	1.1	1.5	0.0	0.0	3.0	4.3
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.6	0.8	0.4	0.6	0.0	0.0	1.0	1.4
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**2.5**	**3.5**	**1.5**	**2.1**	**0.0**	**0.0**	**4.0**	**5.6**

Source: Europe Economics estimates.

The table below contains annual ongoing compliance cost estimates for technical standards on buy-backs and stabilisations. As the costs for issuers are familiarisation and staff training costs, there are no material ongoing costs. There may be some minor training costs associated with the L2 standards for new staff, but evidence suggests this is negligible. For the sell-side, most of the ongoing costs are for maintenance of IT systems. Again, however, it is not clear how much of this cost should be attributed to the L2 standards versus the L1 requirements. We view these ongoing costs as an upper bound for the true L2 costs.

Table 4.4: Annual ongoing compliance costs for technical standards on buy-backs and stabilisations (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.2	0.3	0.1	0.2	0.0	0.0	0.3	0.5
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**0.2**	**0.3**	**0.1**	**0.2**	**0.0**	**0.0**	**0.3**	**0.5**

Source: Europe Economics estimates.

Other adverse market impacts

Separate from the compliance cost burden, ESMA's draft technical standards may have other, wider adverse market impacts. We have identified three such impacts with respect to technical standards on buy-back programmes and stabilisations.

First, ESMA requires that market participants report transparency disclosures to each competent authority. Stakeholders have already indicated that this arrangement would result in higher costs relative to an arrangement in which they would have to report to only one competent authority. There may be an incentive, then, for issuers — where they are listed on multiple venues — to conduct buy-back programmes on a single market or a limited set of markets so as to reduce compliance costs. Similarly, issuers and sell-side institutions may have an incentive to conduct stabilisation purchases on a limited set of markets. Even more extreme, issuers may wish to list on a limited set of markets, avoiding any possible need for price-supporting purchases on several different markets.

The risk, then, is that the requirements could create a "two-tiered" capital market structure within Europe. In one set of markets, share buy-backs and stabilisation purchases would be relatively common. As a result, the market would be more liquid, the price mechanism better-functioning, and these markets would be likely to attract more issuance activity. The second set of markets would become less liquid, the price mechanism would be less informative, and issuers would gradually prefer to engage the first set of markets when borrowing from capital markets. Such an arrangement would also reduce the allocative efficiency of capital markets from a pan-European perspective.

Feedback from stakeholders on this point was mixed, but pointed to a rather minimal impact. On the one hand, some sell-side firms argued that they might advise their clients to focus on one market or a very limited set of markets when conducting buy-backs or stabilisations due to the need to report to different competent authorities. On the other hand, other sell-side firms said that they would inform clients of higher reporting costs when conducting buy-backs or stabilisations in various jurisdictions, but that this would be a relatively minor concern in light of other factors driving buy-back or stabilisation strategy. In general, sell-side and issuer stakeholders were of the opinion that, although they would have preferred reporting to a single competent authority, the requirement to report to multiple competent authorities would probably not have material impact on their buy-back or stabilisation operations. Thus, the wider impacts mentioned above, while theoretically possible, are unlikely to occur.

A second potential adverse impact is the possibility for regulatory arbitrage. For example, if potential market abusing actors (e.g. those trading on inside information) are aware that some competent authorities are less experienced in processing transparency data, do not have sufficient resources to monitor the market, or may be overwhelmed by their responsibilities in regulating buy-back programmes and stabilisations, then the markets that these competent authorities regulate may be targets for market abuse. Although the responsibilities will be largely the same as those under the MAD, the requirement to report to several competent authorities might lead to higher workloads for some competent authorities. Alternatively — and in contrast to the first scenario — one could argue that issuers or financial services institutions may be more willing to list in capital markets where the competent authority's actual or perceived ability to effectively monitor the market is lower and therefore the likelihood of being caught when breaching buy-back or stabilisation requirements is lower. We consider this to be largely a hypothetical risk, as issuers and the buy-side typically prefer transparent and sound markets.

Third, ESMA explicitly notes that buy-backs must be conducted on a trading venue, and not OTC markets, to enjoy safe harbour status. This could create a bias against OTC markets, as investors who trade securities primarily on OTC market will not be able to benefit from the additional transaction activity associated with the buy-back programme.

Our research indicates that this is not a significant concern. No stakeholders believed that ESMA's technical standards would create such a two-tiered capital market structure over and above investors' existing preferences, and we do not consider such a consequence plausible.

4.2 Market soundings

The MAR defines a market sounding as "a communication of information, prior to the announcement of a transaction, in order to gauge the interest of potential investors in a possible transaction and the conditions relating to it such as its potential size or pricing, to one or more potential investors."[22] The entity that makes a market sounding is a "disclosing market participant" (DMP).

Market soundings can contain inside information and, for that reason, can constitute or lead to market abuse. To protect themselves from such charges during the course of legitimate business activities, DMPs are required to comply with ESMA's technical standards on market soundings.

22 Article 11(1) of the MAR.

4.2.1 Technical standards

ESMA's technical standards can be broken down into two broad categories. These are standards relating to activities prior to conducting market soundings and requirements and procedures when conducting market soundings.

We describe each in turn below.

Activities prior to market soundings

Article 11(3) of the MAR obliges DMPs to assess whether or not information to be contained in a market sounding is indeed inside information and to keep written documentation on the reasons underlying the conclusion of this assessment.

These obligations fall on the DMP and are further specified in the technical standards. The assessment will also involve determining when the transaction related to the market sounding is estimated to be made public although there will be no agreed "cleansing strategy" with the potential investor with respect to inside information in market soundings. Nevertheless, the DMP is required to inform the sounded party when information ceases to be inside information, according to Article 11(6) of the MAR. The DMP is required to keep a record of the pre-market sounding due diligence and disclosure proposals. If the related transaction is being arranged by a syndicate, the DMP should ensure that all syndicate members agree about the characterisation of information as non-inside information. If syndicate members cannot agree on the characterisation, the information will be treated as inside information for the purposes of market soundings.

ESMA has not given explicit recommendations on the number and type of investors to question, other than offer some best practice guidance.[23] Additionally, ESMA notes that the time between the market sounding and the anticipated transaction date should be minimised, but does not provide precise requirements for how long the time should be or how it should be minimised.

Requirements and procedures when conducting market soundings

DMPs will be required to obtain potential investors' permission to receive inside information related to a transaction prior to making a market sounding. This relates to any one specific transaction, but DMPs are also required to maintain a list of potential investors who have said that they prefer not to be sounded in relation to potential transactions in general. DMPs do not need to continuously contact investors to query their preferences, but should update the list upon information provided by the potential investors should their preference for receiving market soundings change.

Records kept during the market sounding process are required to be kept in a durable medium. DMPs will need to keep records on all market soundings, not simply those containing inside information.

DMPs are required to develop and maintain a standardised template for conducting market soundings (i.e. scripts). This applies to all market soundings, whether or not they contain inside information. All market sounding scripts are required to contain:

- A statement noting that the communication is a market sounding.
- A confirmation that the DMP is communicating with the appropriate individual.

In the case of a market sounding that contains inside information, scripts will contain:

- A statement that the DMP has assessed the information contained within the sounding and has deemed it to be inside information.

[23] For instance, a syndicate should ensure that a single investor is not questioned by several different syndicate members about the same transaction.

- A reminder to the potential investor that acceptance of the market soundings obliges the potential investor to keep the information confidential.
- The expected time when the information will cease to be inside information, with a note that this time is subject to change and how the potential investor will be informed when this time changes.
- A reminder to the potential investor that administrative and criminal penalties may apply if the potential investor violates laws regarding inside information.
- A request for consent from the recipient of the market sounding to receive inside information.

In the case of a market sounding that does not contain inside information, scripts will contain:

- A warning to potential investors that, although the DMP has judged the information contained in the market sounding not to be inside information, this could be an incorrect assessment and could become inside information when combined with other information held by the potential investor.
- A statement clarifying that the potential investor must assess the information to determine whether or not information in the market sounding is indeed inside information and, if the potential investor concludes that the information is inside information, the potential investor is bound by legal restrictions regarding inside information.
- A request for consent from the recipient to be sounded.

DMPs are required to keep lists of individuals that have received the market sounding. This list contains individual information only on the individual that received the market sounding, rather than employees to whom the market sounding information was subsequently distributed. The list will contain:

- Names of the firms and individuals at the firm who were sounded.
- The date and time of the initial sounding and any follow-ups.
- Contact details employed in the sounding.

The DMP will maintain contact details for a point of contact at potential investors for market soundings and will contact only that individual for market soundings (unless such information is out of date).

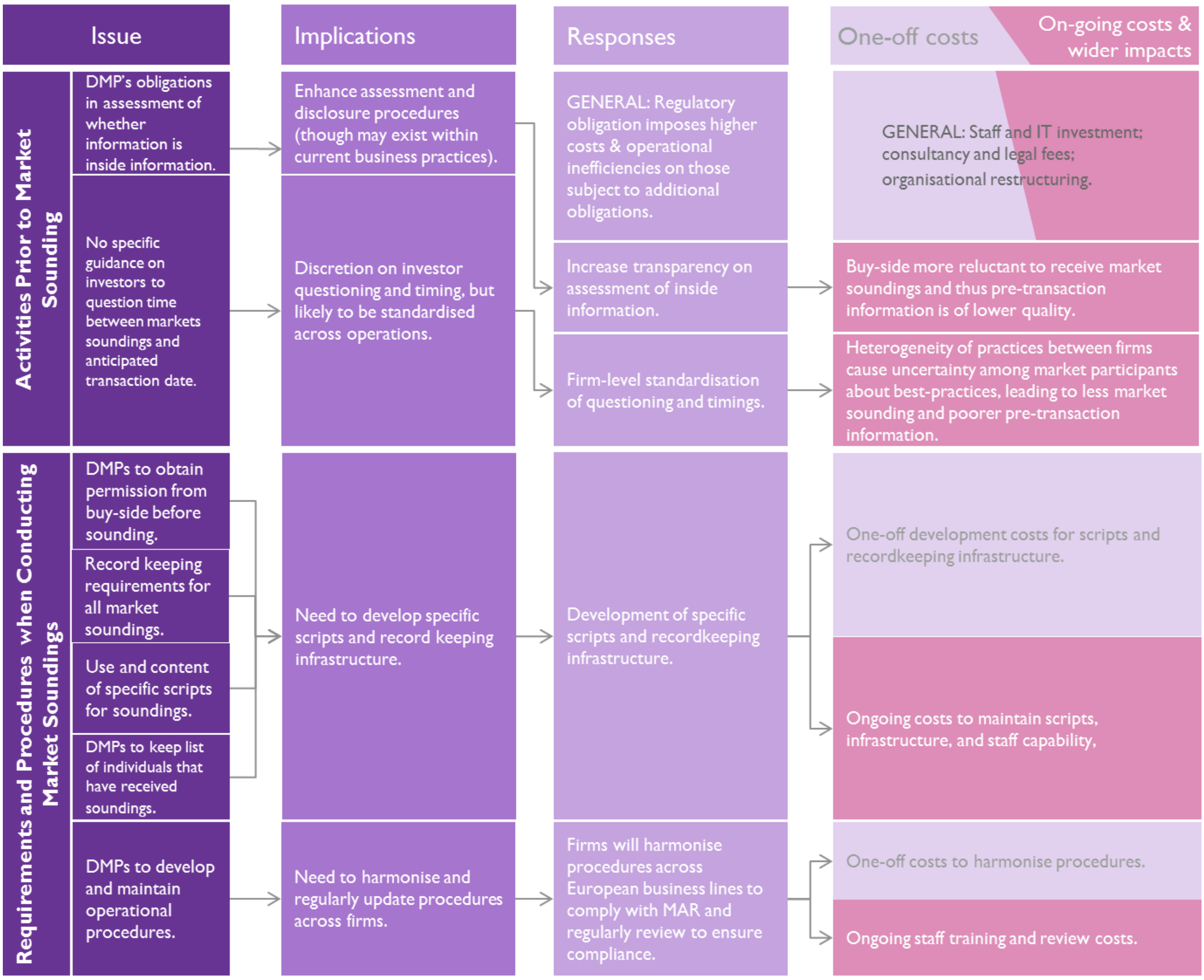
All market sounding communication between DMPs and potential investors must be recorded. For fixed line and mobile telephony, this must take the form of recording conversations. For meetings, a sufficient written account of the items discussed and the conclusions of the meeting must be kept as well as information on dates, times, meeting attendees, and confirmation that content of the market sounding script was shared with potential investor. The content of the meeting record should be confirmed by all parties involved, such as obtaining signatures of potential investors. Alternatively, meetings can also be video recorded, in which case a signature would not be necessary.

DMPs are required to develop and maintain operational procedures for conducting market soundings. These procedures must be reviewed periodically and updated as needed. DMPS are required to take the necessary steps to:

- limit the employees involved in conducting market soundings;
- ensure that these employees have proper training;
- limit the number of employees that have access to information contained in the market sounding; and
- reduce the time between disclosing information to employees conducting market soundings and sounding potential investors.

4.2.2 Mechanisms of effect

Figure 4.3: Mechanisms of effect for market soundings



Source: Europe Economics.

4.2.3 Compliance costs and other impacts

Compliance cost impacts

The primary direct costs will fall almost exclusively on DMPs, which are most likely to be sell-side institutions or issuers when conducting the market sounding. ESMA's guidance and technical standards explicitly reference staff training and IT systems investment as potential costs. Further costs will arise with respect to operational restructuring and updating costs, such as maintaining or updating market sounding scripts.

Sell-side institutions and issuers

Most of the responsibility for compliance with the MAR in respect of market soundings falls on the DMPs. As the DMPs, sell-side institutions and issuers are likely to bear the bulk of the costs arising from the technical standards.

Sell-side institutions and issuers will need to train or re-train staff involved in the market sounding process. It is likely that there will be three classes of staff to be trained, each with potentially different training costs.

First, general compliance staff will need to become aware of firm-level and individual-level requirements on market soundings. This would be primarily a one-off staff training cost.

Second, staff making market soundings will need to be aware of a raft of requirements stemming from the MAR and ESMA's technical standards in particular.[24] This will include, *inter alia*, the design and use of scripts during market soundings and the appropriate records to keep before, during, and after soundings.

Third, staff not directly related to the market sounding process but possessing information contained in the market sounding will need to be trained on obligations stemming from the MAR and in particular ESMA's technical standards.

Sell-side institutions and issuers will be required to keep records on potential investors, including information on who does and does not give consent to be sounded, information on the context and content of market sounding communications, and information on who has been sounded and thus may hold inside information. All of this entails potential IT investment costs and is likely to be a significant cost driver. A list of potential costs includes:

- Voice and audio visual recording and storage — Sell-side institutions and issuers will need to keep voice records of market soundings. Additionally, sell-side institutions may also wish to film in-person meetings when conducting market soundings. Firms may need to invest in recording and storage capacity to keep these records.
- Due diligence records — Sell-side firms and issuers are required to keep due diligence documentation on the determination of whether information in market soundings is inside information. A storage system may need to be designed to facilitate compliance with this requirement.
- Script storage and maintenance — Sell-side firms and issuers will need to use a standardised script when conducting market soundings. This script must be reviewed periodically to ensure that it is sufficient to ensure compliance. Firms may need to invest in IT capacity to store and display market sounding scripts, as well as make them available for period review.

Systems investment would contain a one-off element for the development of the system itself and an ongoing element for maintenance, troubleshooting, and further technical enhancements. Other costs, such as legal services or consultancy services, may also arise.

Some DMP respondents, both issuers and sell-side firms, noted that there were a few aspects of ESMA's proposed technical standards that would result in what they felt were disproportionate costs. These fall into two broad categories.

- First, DMPs thought that the need to hold records on non-inside information soundings as well as inside information soundings was disproportionate. They argued that this would be operationally cumbersome and offer little benefit to the wider market.
- Second, where a sounding was a joint communication between an issuer and its sell-side adviser(s) (e.g. during a conference call), DMPs commented that it was unnecessary for both the issuer and its adviser(s) to hold records of the sounding. Instead, they contended that it would be sufficient for one appointed DMP to hold records. In their view, duplicating records across all DMPs would necessarily lead to additional compliance costs.

Non-bank brokers and dealers

Non-bank brokers and dealers are unlikely to incur further costs.

[24] We mention the wider requirements of the MAR as part of the costs that will arise, but we are investigating the costs of training staff on just ESMA's technical standards.

Buy-side

Buy-side firms are unlikely to incur considerable further costs. Of the compliance costs identified, firms noted that they would need to train a particular set of staff on requirements for receiving market soundings and the expectations they should have from the sell-side when approached to receive a sounding, which are specified in the L2 text. Furthermore, these firms may also have to incur some relatively minor IT costs, mostly associated with recording. As an example of the sort of investment that would be required, one stakeholder said that they might need to invest in approximately ten recorded mobile phones for their capital markets business. This is a fairly minor IT investment since, according to stakeholders, a lot of the existing arrangements will satisfy the L1 and L2 requirements.

Both sets of costs — staff training and IT investment — were deemed to be small and relatively trivial. This is reflected in the low cost figures reported.

Competent authorities

Competent authorities are unlikely to incur further costs.

Trading venues

We do not anticipate trading venues would incur any incremental costs as a result of these technical standards. We note that some survey respondents did apportion cost impacts in relation to familiarising compliance staff on the regulation. However, as the regulation does not concern trading venues directly, we do not foresee this as a material incremental cost over and above any familiarisation with those aspects of the Standards that do concern trading venues. As a result, we do not believe that trading venues will incur compliance costs in any systematic way.

Quantitative compliance cost estimates

In sizing the market impacted by standards on market soundings, we have applied the same logic used for sizing the market impacted by standards on buy-backs and stabilisations. This is because sell-side firms will almost certainly need to have corporate capital markets clients to have the need to conduct market soundings. Issuers will also probably need to conduct market soundings where they are testing market appetite for an intervention, such as an IPO, new issuance etc. Therefore, we continue to use 24 large and 89 medium-sized sell-side firms, along with 100 large issuers and 450 medium-sized issuers, as our population estimates.

Since, in principle, any buy-side firm could be sounded, we have used the full buy-side population estimate of 3,200. For trading venues there is no affected population.

Although we do not have a robust basis for breaking these costs down between equity and debt, qualitative evidence from sell-side firms suggests that much of the costs could accrue to the debt side of their capital markets operations. This is because most firms' equity operations are already sufficient to comply with ESMA's proposed technical standards. Debt operations, however, are less formalised. Many stakeholders were of the opinion that, despite the costs, it would be useful to have more formalised and harmonised market standards for debt soundings.

For the remaining stakeholder groups, costs tended to relate to familiarising the business with the regulation and training staff on how to comply with the regulation. As such, these costs are relatively minor and in some cases less than €1,000 on a per firm basis. For the buy-side, in addition to the familiarisation and training costs, there will be some minor investment in IT infrastructure. Compared to the sell-side, though, this will be considerably less, since the investment will be on a qualitatively different scale (e.g. investing in some recorded mobiles versus developing and maintaining a centralised database).

Table 4.5: Per firm one-off compliance costs for technical standards on market soundings (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	194.8	331.0	29.2	49.7	0.0	0.0
Buy-side	2.5	3.2	0.4	0.5	0.0	0.0
Issuer	9.9	14.8	1.7	2.6	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Table 4.6: Per firm ongoing compliance costs for technical standards on market soundings (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	29.5	57.7	4.4	8.7	0.0	0.0
Buy-side	0.5	0.6	0.1	0.1	0.0	0.0
Issuer	29.1	39.4	5.1	6.9	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

One driver of these costs is of course the proportion of soundings within scope. If not all market soundings required records to be kept, this would likely impact on the ongoing compliance cost. The need for one-off investment in a new IT system would likely be largely unchanged. However, a reduction in the amount of market sounding that must be recorded would reduce the ongoing storage costs.

Table 4.7 gives estimates for the one-off compliance costs arising from technical standards on market soundings. Evidence indicates that sell-side firms will bear the bulk of the costs. Sell-side firms' costs will mostly be in IT investment to organise and store information on pre-sounding due diligence and market sounding transmissions. Furthermore, firms expect that they will need to invest resources in developing and maintaining sounding scripts. Firms mentioned staff training and additional due diligence prior to making soundings, but these were relatively minor, particularly in view of the IT and script costs.

Table 4.7: One-off compliance costs for technical standards on market soundings (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	4.7	7.9	2.6	4.4	0.0	0.0	7.3	12.4
Buy-side	0.1	0.1	0.1	0.1	0.1	0.1	0.3	0.3
Issuer	1.0	1.5	0.8	1.2	0.0	0.0	1.8	2.6
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**5.7**	**9.5**	**3.5**	**5.7**	**0.1**	**0.1**	**9.3**	**15.3**

Source: Europe Economics estimates.

Annual ongoing costs in aggregate are higher among issuers. This is prima facie somewhat incongruous, given that they did not report large one-off costs. Interview data suggests that they view some of the cost items, such as developing and maintaining compliant scripts, as primarily ongoing, while sell-side firms viewed the same costs as having a sizable one-off component (e.g. separating the development costs from the maintenance costs). Ongoing costs relate to maintaining and revising scripts, which would be relevant to issuers as DMPs. Still, these costs are relatively small on a per firm basis. Some of these costs could also relate to storing script-related and transmission-related sounding information. Similarly, sell-side firms will realise ongoing costs for maintaining IT systems and market sounding scripts, with some fairly minor costs for additional pre-sounding due diligence on information. The principal reason the aggregate costs are so much higher for issuers than for sell-side firms is that the affected issuer population is around five times larger than the affected sell-side populations; the per firm costs are comparable.

Ongoing buy-side costs would be extremely minor and would stem from maintaining IT infrastructure for soundings.

Table 4.8: Annual ongoing compliance costs for technical standards on market soundings (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.7	1.4	0.4	0.8	0.0	0.0	1.1	2.2
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.1
Issuer	2.9	3.9	2.3	3.1	0.0	0.0	5.2	7.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**3.6**	**5.3**	**2.7**	**3.9**	**0.0**	**0.0**	**6.4**	**9.3**

Source: Europe Economics estimates.

Other adverse market impacts

The most apparent potential adverse impact relates to the lack of a cleansing strategy with respect to inside information in the market sounding. In the November 2013 Discussion Paper, ESMA proposed a number of options for a "cleansing strategy" that would give assurance to the buy side that inside information communicated in a market sounding is no longer privileged information and that the buy side can resume trading in securities to which the information related.

The L1 MAR text requires DMPs to inform sounded parties of when information ceases to be inside information. Whilst a pre-defined cleansing strategy *ex ante* to allow sounded parties to trade without confirmation from the DMP could be of value to the market, ESMA has no mandate on this and has removed from the draft Standards the potential cleansing strategy options described in the Discussion Paper.

The buy-side bears the risk of receiving a market sounding and, to the extent that it must also conduct its own assessment of the information, judging when it can resume trading in affected shares. ESMA notes that "potential investors will always have the option to decline a sounding if the risk [of trading before market sounding information ceases to be inside information] is deemed too high."[25] This may lead to risk-averse buy side institutions ceasing to participate in pre-transaction information gathering exercises, judging that the risk of participation outweighs any potential benefit. In theory, this situation could have myriad costs. First, issuers and DMPs would be adversely impacted as the quantity and / or quality of the pre-transaction information would be lower. Issuers' expectations of the appropriate price, quantity, and features of issued securities would be less accurate. DMPs' inability to accurately judge market expectations would lead to lower quality bids at the service tendering stage and more uncertainty in the issuance process. Securities issued in such conditions could be more volatile and illiquid, possibly deterring investors. Overall, pre-issuance information would be poorer, which could lead to sub-optimal capital market activity, higher volatility, and lower market efficiency. We note that this situation pre-exists the Technical Standards.

Our research found that many buy-side participants already have misgivings about being sounded and that the lack of a cleansing strategy could exacerbate them. They raised three key issues.

First, some buy-side participants did not feel that the conditions associated with being sounded, such as restrictions on trading, were worth the participation in pre-transaction information gathering processes.

[25] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p30.

This is particularly relevant for smaller buy-side firms and active funds that are keen to avoid being on the "wrong side" of market movements while being unable to trade.

However, we found larger buy-side firms to be less concerned in this regard. Large firms tend to have separate "internally wall-crossed" teams that receive soundings and then sound other individuals within the firm selectively, i.e. they can more easily manage the flow of information. There is also a distinction between active funds and passive funds, with the latter not being able to be sounded as they must continually deal in securities to track an index. These two arrangements allow larger firms to be sounded without restricting trading activity across the entire firm.[26]

Second, buy-side firms noted that the use of scripts did not prevent an individual making an unsolicited market sounding to the buy-side, which created operational difficulties for the buy-side. What is more, these scripts are too heavily caveated, according to some firms, to give the buy-side much assurance to accept the sounding. Respondents argued that they are biased in favour of the DMP, absolving them of all responsibility if information disclosed as non-inside information turns out to be market sensitive. From the view of sell-side firms, however, the script templates place too much emphasis on the risks associated with a sounding such that a buy-side participant would never agree to accept a sounding.

Firms were not sure what more could be done to ensure that they were inadvertently sounded and said that the required use of specific scripts could help in markets where the sounding process is somewhat less formalised. At present, whereas scripts are a common feature of the UK market, use in the rest of Europe is much less frequent.

Finally, and following from the above, buy-side and sell-side stakeholders highlighted key differences in the sounding process between equity and debt markets. In equity, the sounding process is more formalised and stakeholders generally know what to expect when making or receiving soundings. Furthermore, there is typically more transparency about when information will cease to be inside information. On the debt side, by contrast, market sounding processes are less formalised and stakeholders are less sure about when they can expect to be cleansed. A specified cleansing strategy could help formalise processes in debt market soundings and harmonise processes and expectations across debt and equity.

Buy-side and sell-side stakeholders noted that a cleansing strategy could help remedy these issues, although it would not guarantee that they would change their participation in market soundings. For instance, a clear cleansing strategy could provide more transparency on when a firm could expect to start trading again, offer additional protection against inadvertent sounding above the use of scripts, and harmonise processes across debt and equity operations. Stakeholders also commented that the lack of an explicit cleansing strategy did pose risks to them, but that it could be difficult and overly-prescriptive to specify in advance such a strategy.

Despite preferring a cleansing strategy — if feasible — most stakeholders did not believe that the lack of a cleansing strategy would significantly impact the quality of the information obtained in the pre-transaction information gathering process. Some stakeholders noted that this was possible, but that the lack of such a strategy would not dramatically alter current market practices and therefore the information would probably not be of any lower quality than it is currently. In other words, the marginal impact of ESMA's L2 standards on the quality of information gathered through market soundings would likely be minimal.

[26] Larger firms indicated that this was essential, as they were some of the largest players in the market. They argued that, without these arrangements and thus their participation, pre-transaction information gathering would be significantly more difficult.

4.3 Suspicious transaction and order reporting (STOR)

While not all suspicious transactions will reflect cases of market abuse, by definition they may be indicative of market abuse. It is therefore a requirement of MAR that trading venues "establish and maintain effective arrangements, systems and procedures for preventing and detecting market abuse and attempted market abuse". Those arranging and executing transactions ("firms") also have a similar requirement regarding suspicious transactions and orders. MAD and ESMA guidance has previously addressed suspicious transactions reporting, with ESMA drawing on this work as part of its proposals. The MAR extends the scope of the regime beyond equities and to also include orders.

4.3.1 Technical standards

The reporting obligations

Article 16 of the MAR states that "firms" and operators of trading venues are required to report all orders and transactions which may constitute market abuse. This includes suspicious activities where orders have been cancelled, modified or not executed. Effective arrangements must be in place to detect and report any suspicious orders and transactions. Reporting is also required regardless of whether a transaction takes place on a trading venue or OTC.

Timing and level of suspicion required

Articles 16(1) and (2) require reporting of suspicious transactions to occur "without delay". In reality, in the discussion paper ESMA indicates that "without delay" would generally be understood to mean that the Competent Authority is notified within two weeks of suspicion being aroused, but this is not a prescriptive requirement. ESMA states that STORs may be reported by telephone and then followed up with written confirmation in the appropriate form in order to facilitate the timely reporting of STORs.

There will be no "batching" of reports, where a market participant waits until a sufficient number of suspicious transactions or orders have been submitted before notifying a Competent Authority.

ESMA suggest that entities should only base their suspicion on what they observe, rather than what they may infer, such as if they are aware that a client is using multiple brokers. Where a chain of market participants are involved in a transaction, they all have an obligation to make STORs, rather than one entity in the chain absolving the other entities from this responsibility.

Detection

Article 16 requires firms to have systems and procedures in place which aim to detect suspicious market activity. Although for smaller entities ESMA does not require this system to be automated, above a certain size, firms may be required to implement automated systems in order to comply with the regulation. Besides, firms will need to have appropriate training of their staff to develop a proper detection and reporting culture but ESMA is not prescribing details of this as it needs to be tailored to the size of the firm.

Content of STORs and STOR template

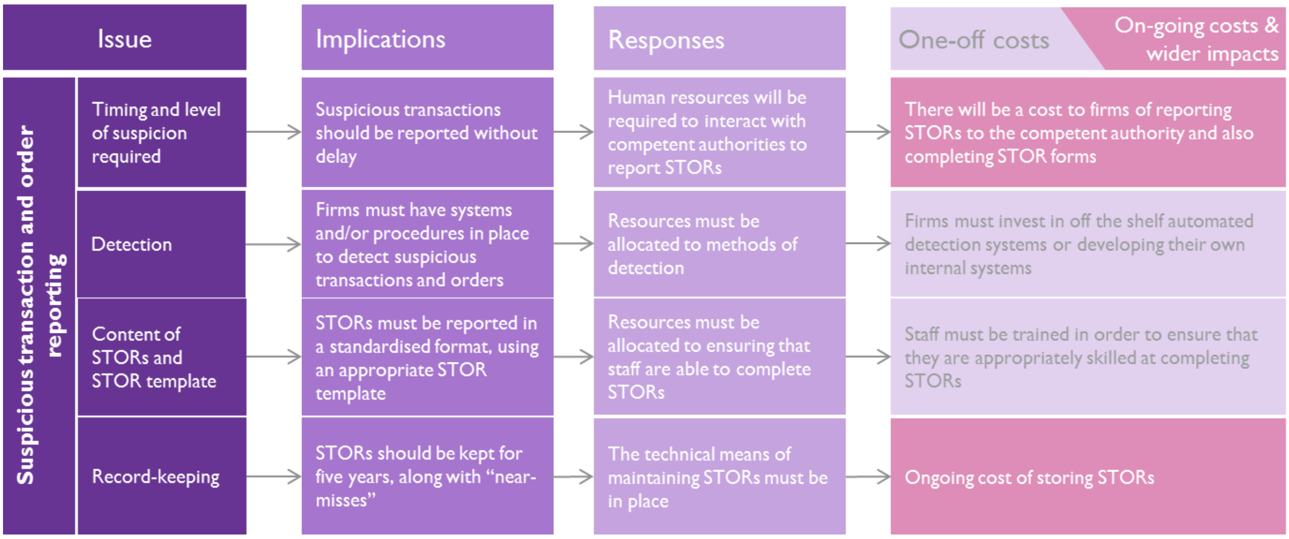
As required under Article 16(5), ESMA is proposing a notification template for STOR. The proposed single harmonised reporting form, in electronic format, allows firms and trading venue operators to fulfil the requirements of Articles 16(1) and 16(2) and is structured in such a way that the relevant Competent Authority is able to easily follow up on any reports or share it with other authorities.

Record-keeping

ESMA proposes that a record of STORs should be kept for five years. "Near-misses", where potentially suspicious transactions which have been examined but not deemed sufficiently suspicious and so are not reported to a relevant Competent Authority, should also be maintained since these should provide some indication as to whether firms are in compliance with the technical standards.

4.3.2 Mechanism of effect

Figure 4.4: Mechanisms of effect for suspicious transaction and order reporting



Source: Europe Economics.

4.3.3 Compliance costs and other impacts

Non-EAMP issuers

Issuers are unlikely to incur further costs, with the exception of EAMPs, which we cover below.

Buy-side, sell-side institutions, non-bank brokers and dealers, EAMPs, and trading venues

The primary cost driver for trading venues and investment firms is likely to concern the detection of suspicious market activities with respect to the extension in scope due to the MAR. However this extension of scope is due to L1. It is important to note that the L1 standards already stipulate the use of a system for STORs, with L2 only specifying the automation of this system. However, it is inherently difficult to separate out these costs, as firms would invest in a new automated system which encompasses both the L1 and L2 costs as one expenditure. The disentanglement by survey respondents was particularly difficult here, and the corollary of this is that there is a material risk of over-statement of the incremental costs solely attributable to L2.

Many firms were concerned about what an automated system actually entailed, as the text in ESMA's proposed technical standards, in their view, did not provide sufficient guidance on the expected features or minimum requirements for such a system. Furthermore, non-trading venue stakeholders all commented that the requirement for and use of an automated system in conjunction with human analysis of trading activities would represent a new and potentially costly regulatory requirement. Stakeholders also argued that ESMA did not provide enough detail on the scope of such surveillance. Stakeholders told us that these sources of ambiguity have made it difficult for them to provide accurate cost estimates and that the costs, particularly on IT investment, will be proportional to the requirements for the automated system and the scope of activities it is to monitor.

Creating and maintaining systems to detect suspicious activity will result in both one-off and ongoing costs for investment firms. Small and large investment firms may face significantly different costs with regards to detection. Since larger firms will typically engage in transactions of greater complexity and because interaction between front office and middle/back office staff may be more limited it is likely that these firms will be required to implement automatic monitoring systems in order to comply with the technical standards. Where smaller firms invest in automated systems, their simpler operations may mean that they are able to purchase off-the shelf systems, rather than developing their own bespoke monitoring systems.

In order to ensure that staff have an understanding of what suspicious activities look like, it is also necessary to provide them with appropriate training. This is particularly important given that "experience of some competent authorities is that some of the very best ST[O]Rs come from the front office staff".[27]

With respect to 'without delay', some firms argued that the two week window, even if not prescriptive, could be too tight. Such respondents may need to invest in more human resources if they still seek to meet this requirement.

Once potential suspicious activities have been detected, entities will next be required to conduct an investigation in order to conclude whether they are actually suspicious activities to report or so called "near misses". Furthermore, firms will have to keep records of detection and investigation of near misses. These records will have to be maintained for a minimum of five years. Both of these costs are directly attributable to the L2 technical standards. Firms will also be required to use a specified STORs template, which could impose some minor one-off adjustment costs while firms become accustomed to this new template (but also enable firms to access ongoing savings once implemented). This could be in the form of a short training session and/or the internal circulation of guidelines on how to fill out the new STORs templates.

The final cost regarding the reporting of STORs relates to the administrative burden of completing the relevant report. This is likely to be an ongoing cost directly proportional to the frequency with which STORs are detected.

Competent authorities

L2-related costs for competent authorities are likely to be relatively minor. They are likely to incur some staff training costs, particularly for how their staff should receive and process reports from market players. Furthermore, competent authorities may have to invest in IT infrastructure for the secure receipt of STORs.

The impact of changes to reporting requirements is not clear. STORs templates and required pre-reporting investigation processes are meant to increase the number of high-quality reports and decrease the number of low-quality reports sent to competent authorities. Therefore, over the medium-term, certain aspects of the L2 standards on STORs templates could *decrease* competent authorities' costs.

Quantitative compliance cost estimates

For STORs-related technical standards, the impacted population for sell-side firms, buy-side firms, and trading venues is the entire market. The affected population of issuers are those non-financial corporates that trade in securities, which we assess would primarily or even exclusively be EAMPs. According to emissions market data firm Carbon Markets Data, there were around 900 firms that are part of the EU ETS. Of these, only the minority (generally speaking the largest energy firms) will be active trading participants in emissions allowances, and so relevant here.

Buy-side firms reported no costs. EAMPs, referred to in the table as issuers, will incur primarily storage-related costs and costs to increase their capacity for reporting to competent authorities and investigating suspicious behaviour and near-misses. EAMPs raised in qualitative terms the possibility that they would

[27] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation".

have to invest in IT systems to meet the automated surveillance requirements, but no EAMP respondents gave cost estimates or even indicated on the survey materials that it would incur further IT costs.

For trading venues, costs were motivated by additional expenditure on record storage, increasing the reporting capacity to competent authorities, and staff training. Most trading venue stakeholders said that ESMA's proposed technical standards on STORs would not imply any incremental IT investment since trading venues currently have sophisticated automated surveillance systems and follow-up on activities with human investigation.

Table 4.9: Per firm one-off compliance costs for technical standards on STORs (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	233.9	334.2	35.1	50.1	3.5	5.0
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	12.6	17.1	2.2	3.0	0.2	0.3
Trading	73.2	99.0	11.0	14.8	1.1	1.5

Source: Europe Economics estimates.

Table 4.10: Per firm ongoing compliance costs for technical standards on STORs (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	106.7	153.0	16.0	23.0	1.6	2.3
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	15.5	21.0	2.7	3.7	0.3	0.4
Trading	57.9	78.3	8.7	11.7	0.9	1.2

Source: Europe Economics estimates.

Below we give the aggregate one-off compliance costs for technical standards related to STORs. The largest aggregate costs are for sell-side firms. The greatest cost impact comes from investment in IT systems, of which the bulk of the costs are investing in a system to meet the automated surveillance requirement. Following that, increasing reporting to competent authorities and staff training are the second and third largest cost drivers, respectively. Additional investigation of suspicious activities and near-misses is a key cost driver. Storage of information for five years will add to compliance costs, but it is a less significant cost driver than the aforementioned drivers. The aggregate costs are highest for small firms simply because the impacted population is around ten times larger than the impacted large and medium-sized population.

Table 4.11: One-off compliance costs for technical standards on STORs (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	5.6	8.0	3.1	4.5	18.6	26.6	27.3	39.0
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.3	0.3	0.1	0.1	0.0	0.0	0.4	0.5
Trading	1.5	2.0	0.2	0.3	0.3	0.3	2.0	2.7
Total	**7.4**	**10.4**	**3.5**	**4.9**	**18.8**	**26.9**	**29.7**	**42.2**

Source: Europe Economics estimates.

Annual ongoing cost for STORs-related technical standards are presented in Table 4.12. For the sell-side, the biggest cost drivers will be reporting to competent authorities and the maintenance of IT systems. Less prominent but still adding to the costs is the need to maintain records for five years. Again, the reason the aggregate costs are higher for smaller firms is that the total affected population is substantially larger than the population of large and medium-sized firms.

Those EAMPs affected estimate that the key ongoing cost driver for them will be investigation of suspicious activities followed by additional reporting to competent authorities and maintaining records for an extended period of time.

For trading venues, costs estimates are largely driven by reporting to competent authorities. After this, the key costs drivers are additional investigation of suspicious activities and maintaining an appropriate internal culture among staff. Issuers also report some IT costs, which we understand are primarily related to the storage of records (including of 'near misses').

Table 4.12: Annual ongoing compliance costs for technical standards on STORs (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	2.6	3.7	1.4	2.0	8.5	12.2	12.5	17.9
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.3	0.4	0.1	0.2	0.0	0.0	0.4	0.6
Trading	1.2	1.6	0.2	0.2	0.2	0.3	1.6	2.1
Total	**4.1**	**5.7**	**1.7**	**2.5**	**8.7**	**12.4**	**14.5**	**20.6**

Source: Europe Economics estimates.

4.4 Technical means for public disclosure of inside information and delays

The public disclosure of inside information helps to ensure the efficiency of financial markets, since it enables market participants to disseminate relevant information which should be reflected in the value of financial instruments.

The timely disclosure of inside information also helps to mitigate the likelihood of insider dealing, since it reduces the timespan over which insider dealing may occur.

Article 17 of the MAR expands upon article 6 of the MAD. Issuers of financial instruments are required under the MAR to disclose inside information publicly as soon as possible. Information is also required to be distributed in such a way that it "enables fast access and complete, correct and timely assessment of the information". The disclosure of public information is currently required under MAD by issuers of financial instruments admitted to trading on a Regulated Market (RM). Under the MAR this is to be expanded to include:

- issuers of financial instruments only traded on an MTF where these issuers have requested admission to trading on an MTF or have approved trading on an MTF;
- issuers of financial instruments only traded on an OTF where these have approved trading on an OTF; and
- emission allowance market participants (EAMPs) above the threshold to be set by the European Commission. We estimate this at about 70 firms, of which none — by definition — would be small participants.

4.4.1 Technical standards

ESMA has developed a number of technical standards for the means for public disclosure of inside information and means for delaying the disclosure inside information. We describe each of these means in turn below.

Technical means for public disclosure of inside information

Article 17(1) obliges issuers of financial instruments to disclose publicly inside information as soon as possible in a way that facilitates easy access and complete, correct, and timely assessment of the information by the public. Requirements in Article 17(1) are the same as those under the MAD, so issuers currently operating under the MAD will face similar requirements under the MAR. Issuers covered by the Transparency Directive — i.e. those issuers trading on Regulated Markets — will also need to disclose the inside information in an official appointed mechanism (OAM).[28] EAMPs are also required to disclose inside information publicly, effectively and in a timely manner.

Besides, the MAR requires all issuers, whether subject to the Transparency Directive or not, must post disclosed inside information on their websites and maintain it there for a minimum of five years. For issuers on SME growth markets, the MAR allows these issuers to post the information on the SME growth market's website rather than on their own. ESMA contends "it is assumed that inside information should remain published on the SME growth market operator's website for at least five years". However, EAMPs are not required to post all inside information on their websites for five years.[29]

ESMA proposes that mechanisms, and channels to be used by all issuers under MAR for the public disclosure of inside information comply with the same requirements and standards, relating to dissemination of information as set out in the Transparency Directive. For issuers on Regulated Markets, this implies continuity with current practices. However, for others covered under the MAR, this represents a new requirement. The public disclosure should occur without delay. This also holds for EAMPs without preventing them from using a Regulation on Wholesale Energy Market Integrity and Transparency (REMIT) disclosure channel provided it satisfies these requirements.

Disclosure via other means, such as social media or publication in a newspaper, would not meet the requirements for proper dissemination. Posting inside information on the relevant Competent Authority's website only would not be sufficient to comply with the MAR "unless the Competent Authority's means for disclosure of inside information meet the requirements of proper dissemination and of appropriate public disclosure set out in the [Transparency Directive]."[30]

ESMA notes that "the website where inside information is posted by the issuer in fulfilment of Article 17(1) and 17(9) [of the MAR] should have the following technical features:

- The access to the website should be non-discriminatory and free of charge.
- Inside information should be easy to find.
- Considering the five year record keeping, previously disclosed inside information should be easy to find, for instance via an archive-type tool; disclosed information should notably be clearly dated."[31]

Technical means for delaying the disclosure of inside information

The MAR lays out two types of delays to the disclosure of inside information: "general" delays and delays to preserve the stability of the financial system.

With respect to "general" delays, the MAR requires that Competent Authorities be informed by issuers or EAMPS *ex post* about the existence of a delay and a written explanation on how conditions to be met when delaying the disclosure of inside information were met. The MAR does allow for the possibility of this latter explanation to be provided only upon request of the Competent Authority, if allowed by national law. The existence and explanation disclosures should take place immediately after the information is publicly disclosed.

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28 Issuers on other types of trading venues not covered by the Transparency Directive, such as MTFs or OTFs, do not have to use the OAM, which a storage mechanism under the Transparency Directive.

29 ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p57.

30 ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p54.

31 ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p58.

ESMA considers that the act of notifying the Competent Authority should be integrated into the issuer's general process for disclosing inside information. These notifications should be provided in writing via a secure electronic transmission mechanism to a dedicated contact point at the Competent Authority. The Competent Authority should make the notification process clear to issuers.

With respect to information provided about the delay, ESMA proposes to include the following information in the notification sent to the Competent Authority:

- "the identity of the issuer: full official name;
- the identity of the person within the issuer making the notification (name, surname, position, contact details: emails, professional phone number);
- identification of the disclosed insider information that was delayed (title of the disclosure statement, reference number assigned by the dissemination system if available);
- date and time of the public disclosure of the relevant inside information;
- date and time of the decision to delay the disclosure of inside information; [and]
- the identity of the persons having taken part in the decision making process for delaying."[32]

The time stamp on the communication should specify the time zone and be as granular as possible.

If the explanation is sent after, rather than with, the delay notification, the above information should be provided with the explanation as well.

To demonstrate that the conditions for legitimate delays to disclosing inside information were met, ESMA proposes that issuers submit the explanatory notification around three conditions, completed in free text:

- "describing the legitimate interest at stake;
- specifying [the issuer's] assessment on how the omission of the inside information would not be likely to mislead the public; [and]
- describing how the confidentiality of the delayed inside information is ensured, notably what information barriers have been put in place internally for non-required persons within the issuer vis-à-vis third parties. Without prejudice of the need to identify the persons within the issuer who decided about the delay, it is not considered necessary to name the persons within the issuer who has access to this delayed information, as they should already be included in the insider list."[33]

When there is a change with respect to how the conditions were originally met, a new assessment of the conditions and the assessment's timing should be included in the explanation.

The notification should be drafted in the language in which the inside information is disclosed. The exception to this is notifications for EAMPs, which could either be made in a language accepted by the Competent Authority and a "language customary in the sphere of international finance", or only in the latter.

In terms of record keeping, issuers are expected to have an organisational structure and processes in place to conduct an assessment of whether information is inside information, whether or not to delay disclosure, and, if the issuer decides to delay, how long the delay should be. There should be a responsible person or set of persons with sufficient capacity and seniority to make such a decision within the organisation. It is this person or these persons who conduct an assessment of whether the three criteria under Article 17(4) of the MAR with respect to inside information are satisfied. Furthermore, there should be an assessment of when the delay should end, how the inside information is disclosed, and how disclosure and notification to the Competent Authority has been achieved. The issuer must monitor on an ongoing basis whether the conditions justifying the delay remain. In the event that there appears to be a breach of confidentiality, the information must be immediately disclosed to the public as required under Article 17(7) of MAR.

[32] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p59-60.
[33] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p60.

All of these processes require records to be kept by the issuers. ESMA's draft technical standards propose that the following internal records be kept:

- "the process for assessing and deciding on the starting and ending point of delaying the inside information;
- the fulfilment of the conditions for delay, both initially and on an ongoing basis during the delay period, are set up and kept under regular view (a new record is needed just when there has been a change in the original conditions);
- responsibilities within the issuer are clearly allocated … [and]
- the delayed inside information is properly handled and managed within the issuer as well as with respect to third parties in order to limit to the extent possible, if not avoid, any breach of confidentiality during the delay period."[34]

Additionally, ESMA specifies that the issuer should keep records of the means put in place to:

- "deny access to non-required persons;
- ensure awareness of the persons accessing delayed inside information about the legal and regulatory duties as well as of the sanctions attached; and
- immediately disclose the inside information in case of breach of confidentiality".[35]

ESMA believes that the more individuals that are involved in handling the inside information, the more stringent the processes in place should be.

Delays to preserve the stability of the financial system

For some issuers, specifically credit institutions and financial institutions, the MAR allows for delays to preserve the stability of the financial system. These delays require notification *ex ante* and must be agreed by the Competent Authority in advance. The technical means for recording this type of delay are the same as those for "general" delays. However, given the highly sensitive nature of the information, ESMA suggests the secure communication channels are used between issuers and Competent Authorities.

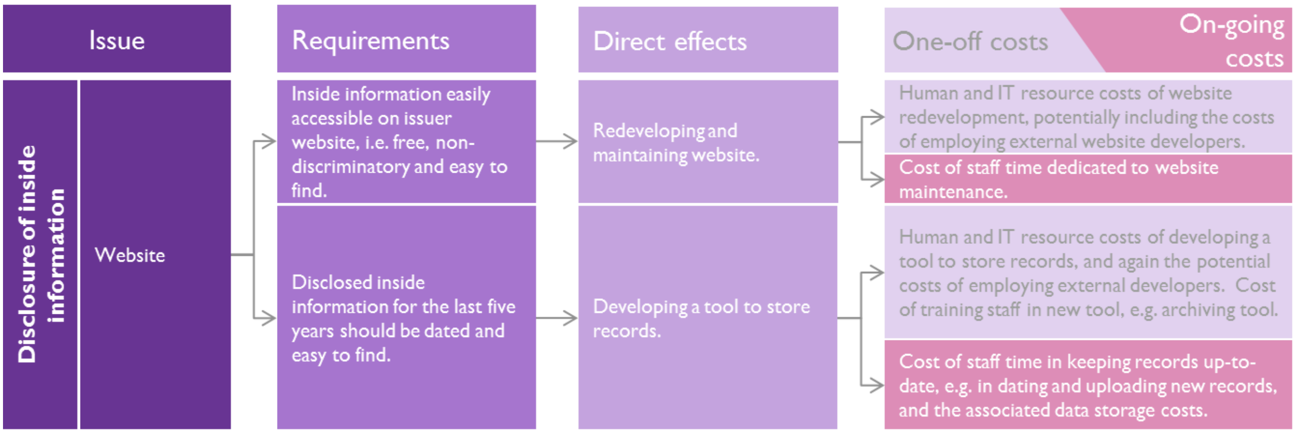
The issuer's notification to the Competent Authority of intent to delay disclosure of inside information should be made in writing. The Competent Authority should inform the issuer of their decision to grant or not to grant consent for the disclosure. This can be done orally initially, but should be followed up in writing without delay.

The issuer and the Competent Authority should inform one another of any new development, event, or information that could affect the fulfilment of conditions for delaying disclosure.

[34] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p62.
[35] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p62.

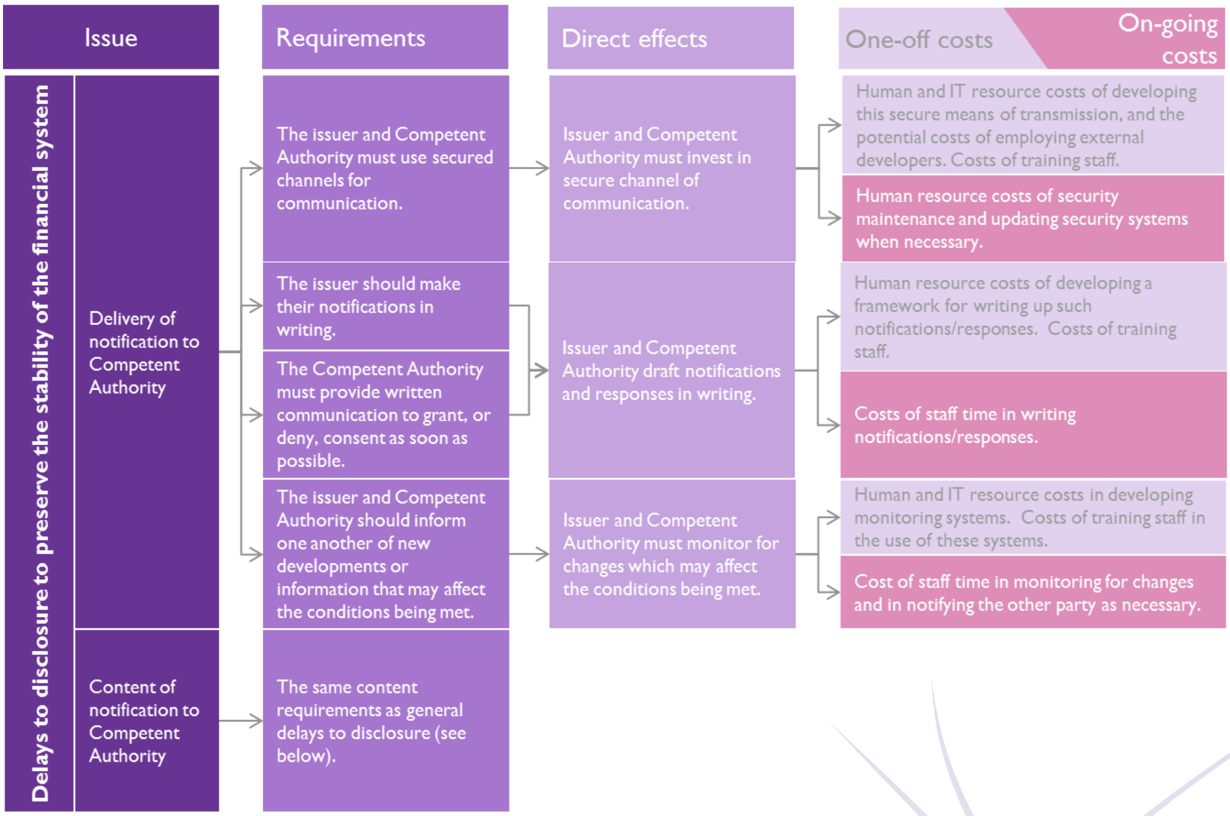
4.4.2 Mechanism of effect

Figure 4.5: Mechanisms of effect for technical means for public disclosure of inside information



Source: Europe Economics.

Figure 4.6: Mechanisms of effect for technical means for delays to disclosure to preserve the stability of the financial system



Source: Europe Economics.

Figure 4.7: Mechanisms of effect for technical means for general delays to disclosure

Issue		Requirements	Direct effects	One-off costs	On-going costs
General delays to disclosure	Delivery of notification to Competent Authority	Notifications to be provided in writing using a secure electronic transmission mechanism.	Issuers develop a secure means of electronic transmission.	Human and IT resource costs of developing this secure means of transmission, and the potential costs of employing external developers. Costs of training staff.	Human resource costs of security maintenance and updating security systems when necessary.
		The issuer should have a dedicated point of contact at the Competent Authority and the Competent Authority should make the process clear to issuers.	Competent Authority assigns dedicated point of contact.	Human resource costs of assigning a dedicated point of contact for each issuer.	
			Competent Authority clarifying process to issuers.		Cost of staff time in clarifying the process to issuers, e.g. through telephone conversations and in writing.
	Content of notification to Competent Authority	Various basic informational requirements for the notification, including the identity of the issuer, the identity of person making the notification and the identification of persons involved in the decision to delay.	Issuers collect and store the information for use in notification when necessary.	Human and IT resource costs of developing a database to store such information.	Cost of staff time in keeping the database up-to-date.
			Issuers draft the notification document with the necessary information.	Costs of training staff in producing the notification document.	Cost of staff time in drafting the notification document.
		Explanatory notification completed in free text and structured around three core issues: describing the interest at stake, explaining how the omission of inside information is not likely to be misleading to the public, and detailing the information barriers in place to ensure confidentiality.	Issuers may need to (re)develop internal information barriers to a sufficient standard, as these barriers must now be disclosed to, and scrutinised by, the relevant Competent Authority.	Human and IT resource costs of (re)developing internal information barriers. Potentially organisational restructuring costs to ensure inside information cannot be accessed by non-required persons and third parties.	
		The language of the notification should match that in which the inside information is disclosed, except for EAMPs which must disclose in a language accepted by the relevant Competent Authority and a language customary in international finance.	EAMPs must translate the notification into other languages, both of which may not be the language in which the EAMP usually operates.	Costs of training staff in relevant languages and/or the costs of hiring staff with relevant language skills.	Cost of staff time in translating the notification document, and the costs of staff time in the quality control of this process.
		A reassessment of the conditions must take place, if there is a change with respect to how the conditions were originally met.	Issuers must monitor for changes which require re-notification to the Competent Authority.	Human and IT resource costs in developing monitoring systems. Costs of training staff in the use of these systems.	Cost of staff time in monitoring for changes and in producing new notification documents as necessary.
		Issuers must ensure that a responsible person is always available to assess whether the three conditions for disclosure (in Article 17(4)) are met, with the decisions and reasons underpinning this recorded.	Issuers must ensure that there is cover in place such that a sufficiently qualified individual is always available to assess disclosure. The responsible persons must have a good awareness of the conditions in order to carry out assessment and must record this decision process in writing.	Costs of training staff with prime responsibility (as well as cover staff) in understanding the three conditions and in how to record this assessment process.	Costs of staff time in assessing against the three conditions for disclosure and in recording this assessment process in writing.
	Internal record keeping	The issuer should have internal records in place to evidence various procedures and structures they have in place to ensure correct delays to disclosure and to ensure confidentiality of inside information during this period.	Issuers keep records on several underlying procedures and structures they have in place.	Costs of training staff in how to carry out this record keeping and the human and IT resource costs of developing frameworks (and storage) for record-keeping in each of the areas specified by ESMA.	Costs of staff time in keeping records up-to-date and costs of additional data storage.
			Issuers may have to improve, and/or develop new, procedures and structures as these could be subject to scrutiny by the Competent Authority.	Human and IT resource costs of investing in improving existing, and developing new, procedures. Costs of organisational restructuring and costs of training staff in light of the new structures and procedures.	Costs of staff time in running these new systems
		The issuer must ensure that their staff are aware of these internal procedures in place.	Issuers must summarise the internal procedures in place and communicate this to staff.	Costs of staff time in producing a summary document and circulating to staff, and possible training costs if necessary.	

4.4.3 Compliance costs and other impacts

Compliance costs

The main costs associated with these technical standards relate to one-off and ongoing human and IT resource costs incurred in implementing and maintaining more thorough reporting and record-keeping practices. The costs predominantly relate to issuers, including emission allowance market participants.

Issuers and EAMPs

These stakeholders are likely to incur the one-off human and IT resource costs of website redevelopment in order to make inside information easier to access, including dated inside information for the last five years (although the five year requirement is an L1 requirement)). Website redevelopment may well also involve the contracting external web-designers to help undertake such changes. The use of external website developers may be more likely in the case of smaller issuers who are less likely to have the expertise in house (a possible exception here being if they are on an SME growth market, which then affords some exemptions stemming from the L1 text).

One-off costs could also include relatively minor costs of training staff in the use of the new website structure, or at the very least disseminating information to staff about the new website structure and its use. Most important in this regard are likely to be training/informing staff about how to upload additional disclosed inside information to the five year online log.

The technical standards relating to delays to disclosure may too impose one-off resource costs. The need to develop a secure electronic channel for communication is likely to incur costs of investing in new IT infrastructure and potentially the costs of external expertise in an advisory and/or set-up role. In addition, there may be some small training costs in bringing staff up to speed with the new system of communication. However, training costs are likely to be higher in the context of improving staff expertise in drafting written notifications, although this may be somewhat mitigated by the internal development of a more prescriptive framework for completing such notifications. That said, the development of such a framework would itself require upfront human resource costs. The need to inform the relevant Competent Authority of developments that may affect the conditions being met could also require issuers to develop internal monitoring systems and processes, which are likely to incur both one-off costs of IT investment and one-off costs of staff training in these new systems and processes.

The various content requirements for the notification of delays to Competent Authorities may also impose material one-off costs. Issuers may need to develop a database to store basic company and employee information, such as list of contact details for persons involved in the decision to delay, so that this information can be disseminated quickly to the Competent Authority when necessary. Issuers may also incur the costs of training staff in preparing such notification documents, particularly with regard to drafting the explanatory free text which provides a rationale for the delay to disclosure. One of the content requirements of the free text is to describe the information barriers in place to ensure confidentiality and, therefore, as the sufficiency of such barriers could now be subject to more scrutiny from the relevant Competent Authority, issuers may deem it appropriate to invest in the improvement of these information barriers. This may include a process of organisational restructuring to ensure greater security of inside information against access by non-required persons and third parties, as well as investment in IT infrastructure.

The requirement for all issuers to make sure that a responsible person is *always available* to assess and record whether, and how, the three conditions for disclosure are met, means that issuers would need at least two members of staff capable of doing so, such that cover can be provided in the case that one of the responsible persons is away. Therefore, issuers may face the costs of training additional members of staff in this role such that there is always an available member of staff to undertake this assessment process.

ESMA's Technical Standards also specify that internal records must be kept to provide evidence of the procedures and structures issuers have in place to ensure correct delays to disclosure and the confidentiality of inside information. This could impose one-off human and IT resource costs required to develop databases, or similar record-keeping tools, as well as then the costs of training staff in the use of these new systems. The issuer must also ensure that their employees are aware of such internal procedures and structures which may, at the very least, incur costs of staff time needed to produce and disseminate a written document explaining these issues, but may also, in some cases, warrant additional staff training.

The costs discussed so far would be applicable across all issuers, including EAMPs. However, regulation differs between these two groups in one aspect, as for all other issuers the language of the notification should match that in which the inside information is disclosed, yet for EAMPs disclosure must take place in a language accepted by the relevant Competent Authority and a language customary in international finance. That said, this requirement is already in place for EAMPs as part of REMIT and, therefore, we do not expect this to impose any incremental costs.

The ongoing compliance costs of meeting ESMA's draft Technical Standards predominantly relate to the costs of additional staff time that will be required to undertake a range of additional functions, namely: keeping databases and other internal records up-to-date; maintaining websites; updating security systems; drafting notifications for delays to the relevant Competent Authority; and monitoring for changes in how conditions for delays are met and reporting as necessary. There may also be some more ad hoc ongoing IT investment costs relating to the improvement of security for electronic transmission and in increasing data storage capacity in light of the new record-keeping requirements.

Our evidence shows that the vast majority of compliance costs will fall on issuers. The key one-off costs are identified as developing IT infrastructure and employing external professional services. Almost all issuers envisaged incurring one-off costs in understanding the regulation and training staff in the regulation. However, the extent of these training costs varied markedly. A large EAMP said that the one-off training costs would equate to approximately 60 man days, while another large issuer said that training would be applicable, to some extent, the whole company, but most importantly the training of the board and the compliance staff. This is contrast to a medium-sized issuer who said that they would incur training costs, but that they would certainly not be material. No issuers anticipate organisational restructuring costs, while only one (an EAMP) expects to have to increase their capacity for reporting to competent authorities.

The key ongoing costs are expected to be the continuing maintenance, and upgrading, of IT infrastructure, and annual training costs (which one respondent anticipates could require up to 30 man days per annum). One respondent, an EAMP, also envisages spending over €1,000 per month on external professional services in this context. However, no standard issuers anticipate costs for utilising external professional support.

Sell-side institutions

Sell-side institutions who are party to the inside information of issuer clients could also incur compliance costs as a result of these technical standards. Although sell-side firms are not directly responsible for disclosure, they may nevertheless be involved in advising issuers on the capital market consequences of disclosing or not. While most sell-side firms acknowledge in the survey that this would impose additional resource requirements on them, the precise nature of these additional resource requirements is more uncertain. There are two measurement issues here. First, some large part of any such cost will stem from the Level 1 requirements, but may nevertheless be somewhat exacerbated by the detail of Level 2. The difficulty in disentangling the incremental costs of L1 and L2 could mean that the quantitative estimates presented at the end of this section are an overestimate of the true cost of the Level 2 standards. Second, there is scope for sell-side institutions to pass on such costs to clients — e.g. by creating in effect a new advisory offering. On the other hand, they may choose to absorb such costs, i.e. as a form of relationship development. This ambiguity introduces additional uncertainty about the *distribution* of the cost impact, since if re-charged the sell-side's costs would increase pro rata.

The quantitative evidence from the survey suggests that the key one-off costs will be those incurred in understanding the new regulation and training staff appropriately. One respondent said that the precise one-off costs will depend on whether the requirements are met manually, or whether they decide to invest in a new IT system. Sell-side firms, like issuers, anticipate the use of external professional services, but this was only thought to be needed on a one-off basis. In this regard, one sell-side firm said that they would need to get lawyers more involved, and especially so in the case of European clients.

One point of caution in this case is that, although we surveyed sell-side institutions to understand the compliance costs in their capacity as a sell-side firm, it may be that some of the compliance costs reported fed through from the firm thinking as an issuer as well as a sell-side firm. We tried to minimise this risk at the interview stage by stressing that we were interested in costs from the perspective of a sell-side firm, irrespective of whether it is an issuer or not, but clearly the risk of contamination of the costs in this way is still a possibility.

Buy-side institutions

It is difficult to envisage any direct compliance costs for buy-side firms as a result of the draft technical standards. This is reflected in the very minor one-off compliance costs obtained through the survey. These costs are limited to the costs of understanding the requirements and training staff accordingly. Given the extremely minor nature of these costs on a per firm basis, this suggests that the buy-side firms appreciate that they are unlikely to be directly impacted by the technical standards. The training process is likely to be brief and limited to a very small proportion of total employees.

However, as with sell-side institutions, we must once again be wary of two key factors that may be influencing these costs estimates:

- Stakeholder confusion about Level 1 and Level 2 standards, and/or difficulty in separating out the costs of Level 1 and Level 2 standards.
- Buy-side firms reporting compliance costs that actually relate to their position as a corporate issuer, rather than purely as a buy-side firm.

Trading venues

We did not envisage any compliance costs arising for trading venues as a result of these technical standards. This is supported by the survey evidence, with trading venues reporting no one-off or ongoing compliance costs.

Quantitative compliance cost estimates

Table 4.13 and Table 4.14 below provide the per firm one-off and ongoing compliance costs. It shows that per firm compliance costs are much higher for sell-side firms on a one-off basis, but fairly similar between sell-side firms and issuers on an ongoing basis. Although the costs to large sell-side firms and issuers may appear high, these costs are certainly not material when considered relative to the operating expenditure of these organisations. Large sell-side institutions and issuers can have operating expenditures well in excess of €1bn and, as such, these compliance costs are likely to represent less than one hundredth of a percent of total operating expenditure.

Table 4.13: Per firm one-off compliance costs for technical standards on the technical means for public disclosure of inside information and delays (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	58.0	49.6	7.4	4.7	0.7	0.5
Buy-side	9.3	12.6	1.4	1.9	0.1	0.2
Issuer	56.2	116.7	9.7	20.2	1.0	2.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

Table 4.14: Per firm annual ongoing compliance costs for technical standards on the technical means for public disclosure of inside information and delays (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	9.3	9.6	1.2	0.9	0.1	0.1
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	9.0	22.6	1.5	3.9	0.2	0.4
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates

Table 4.15 and Table 4.16 show the total one-off and ongoing compliance cost estimates for the technical standards on the technical means for the public disclosure of inside information and delays.

In terms of population sizing, we assume that the entire population of issuers are affected, as the MAR Level 1 requirements have expanded the affected population to issuers on regulated markets and MTFs, and actively trading EAMPs.

Table 4.15: Total one-off compliance costs for technical standards on the technical means for public disclosure of inside information and delays (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	1.4	1.2	0.7	0.4	0.4	0.3	2.5	1.9
Buy-side	0.2	0.3	0.3	0.4	0.4	0.6	1.0	1.3
Issuer	15.2	31.5	18.9	39.5	5.9	12.2	40.0	83.2
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**16.8**	**33.0**	**19.9**	**40.3**	**6.7**	**13.1**	**43.4**	**86.4**

Source: Europe Economics estimates.

Table 4.16: Total annual ongoing compliance costs for technical standards on the technical means for public disclosure of inside information and delays (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.2	0.2	0.1	0.1	0.1	0.1	0.4	0.4
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	2.4	6.1	3.0	7.6	0.9	2.4	6.4	16.1
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**2.7**	**6.3**	**3.1**	**7.7**	**1.0**	**2.4**	**6.8**	**16.5**

Source: Europe Economics estimates.

The compliance cost estimates above show that the majority of the costs are attributable to issuers. Although the per firm costs are higher for sell-side institutions (as seen in Table 4.13 and Table 4.14), the large population of affected issuers means that the total costs incurred across all issuers is much higher. In the case of both issuers and sell-side firms, it is the large organisations that incur the highest costs, despite the small numbers of them.

As aforementioned, there are no compliance costs for trading venues, while the buy-side anticipates only minor one-off costs.

Competent Authorities

Although the compliance costs for competent authorities are not part of the quantitative analysis, there may be some minor compliance costs incurred by Competent Authorities. ESMA's Technical Standards specify that a Competent Authority must assign a dedicated contact point for each issuer and that it is the responsibility of the relevant Competent Authority to clarify the delays process to issuers. The potential compliance costs of the former would depend on what qualifies as a dedicated contact point. If this were merely to require a dedicated email address for issuers then, clearly, there would be no meaningful compliance cost. However, if a dedicated contact point referred to a dedicated employee then competent authorities would incur one-off resource costs associated with assigning an appropriate point of contact for each issuer. It may also introduce operational inefficiencies, as it restricts the flexibility of the Competent Authority to provide points of contact on ad hoc basis in order to better match current resource requirements. The requirement to clarify the delays process to issuers should only translate to minor ongoing costs of staff time in clarifying the delays process to issuers.

In the case of delays to disclosure to preserve the stability of the financial system, Competent Authorities must provide written documentation confirming whether the issuer's request to delay disclosure has been granted. This could impose one-off costs of producing a framework for this documentation and training staff in how to draft this documentation, as well as the ongoing costs of staff time needed to produce the documentation.

Other adverse market impacts

Due to the expanded coverage under the MAR to include issuers outside of Regulated Markets, this could mean that many of the requirements set out in ESMA's draft Technical Standards impose proportionately larger costs on issuers not on Regulated Markets. For issuers on Regulated Markets who are already compliant with the Transparency Directive, the Technical Standards proposed by ESMA are likely to represent more limited incremental change. This could have harmful competitive implications for issuers on non-regulated markets relative to those issuers listed on regulated markets.

The views on this from our fieldwork were mixed. One respondent thought the effect could be significant, with the view that aligning the dissemination requirements would reduce the attractiveness of listing on non-Regulated Markets and hence reduce the number of SMEs who list. This respondent believes disclosure requirements are an important factor in a firm's decision of whether or not to list, particularly for SMEs. It is difficult to anticipate at this stage the likely materiality of this effect. In addition, we note that since the disclosure requirements are L1 requirements, this cannot reasonably be attributed to the L2 standards.

One concern raised was whether the additional requirements imposed by the Technical Standards make the process of applying for delayed disclosure overly burdensome to the extent that some delays, which would be permitted on the basis that public disclosure would prejudice a company's legitimate interests, may be foregone. Again, however, while hypothetically possible, the material costs of notification are unlikely to exceed the potential loss that could result from premature disclosure, and hence it should still be rational for issuers to undertake the notification process. In fact, by improving the transparency of the application and assessment process, the Technical Standards may actually increase the number of delay notifications submitted. Stakeholders did not consider this a risk in practice.

Another issue that arose from both the survey and the existing consultation responses is that MAR could overly burden EAMPs who are already subject to REMIT, without providing a commensurate improvement in transparency and investor access. Many deem this an unnecessary burden due to the very similar content of MAR and REMIT, with the latter already allowing for effective and proportionate disclosure of inside information. Clearly, this additional burden is attributable to both the Level 1 and Level 2 standards, but it is difficult to disentangle the two effects. However, what we can say is that, by adding to the compliance costs, the Level 2 standards will add to the burden of EAMPs already subject to REMIT. Against this, as we have already noted, the disclosure requirement on EAMPs under MAR is subject to a threshold, and that perhaps only 70 EAMPs would be subject to the disclosure requirement.

The concern is that firms who are energy market participants under REMIT and EAMPs under MAR will be subject to duplications of effort and unnecessary cost burdens, due to inability to combine the standards and procedures to meet the similar, but slightly differing requirements, under MAR and REMIT. In extremis, the requirement to publish similar information elsewhere could even be misleading if published in different formats. A few respondents also believed that it would increase the risk of unintended compliance breaches, due to the very similar, but not exact same, requirements of REMIT and MAR. This greater uncertainty is, in turn, likely to complicate the internal surveillance and compliance processes. However, as we have noted already, the disclosure obligation itself is L1.

4.5 Format of insider lists and managers' transactions notification and disclosure

We address the costs relating to the format of insider lists and managers' transactions notification and disclosure in the same section, due to the common cost characteristics that arise with regard to both sets of technical standards. We present the technical standards of each in turn, before discussing the costs simultaneously. That said, we do present separate compliance cost estimates for each of the areas of technical standards.

4.5.1 Technical standards — insider lists

The creation, maintenance and update of insider lists is a means of detecting and preventing individuals with access to inside information from utilising this information to their benefit, such as for unfair gain. Article 18 of the MAR specifies the creation of such lists comprising all individuals directly employed by issuers, or else engaged in an indirect role, such as accountancy or advisory services. The insider list requirements also apply to EAMPs, auction platforms, auctioneers, and the auction monitor. ESMA, in turn, has drafted technical standards regarding the specific format of these insider lists and the means by which they must be updated. Mechanisms of effect and our discussion of costs and wider effects are included with our discussion of PDMR templates/ notifications in Section 4.5.2.

Content

Article 18 specifies that the insider list should include the identity of any individual with access to inside information. In this regard, ESMA has specified that the following personal information should be disclosed in insider lists[36]:

- Name: first name, surname and birth surname.

[36] Issuers on SME growth markets are exempt from maintaining a contemporaneous insider list under Article 18 of the MAR. See below the section on the exemption for SME growth market issuers.

- Full home and work address.
- National Identification, or the date and place of birth (this will depend on the Member State).
- Home, work and mobile telephone numbers.
- Personal and work e-mail addresses.

The function of each insider must also be specified, as well as the company name for those insiders employed by third parties working for the issuer. The insider lists must also specify the exact date and time (including time zone) at which the individual gained access to the inside information in question, and the exact date and time at which access to this information ended.

Coverage

In terms of the types of person with access to inside information that must be included in insider lists, ESMA proposes the following:

- Member of the management and/or supervisory board.
- Executive officers.
- Individuals discharging management responsibilities.
- Related staff members (e.g. personal assistants).
- Internal auditors.
- Individuals who can access information on budgets and balance sheets.
- Individuals operating in areas with regular access to inside information.

Third party professionals subject to the regulation include: auditors, attorneys, accountants, managers of issuers, ratings agencies, investment analysts and tax advisors. ESMA's list in this regard is to be considered indicative and non-exhaustive.

Format of the insider lists and delivery

ESMA adopts a flexible approach to how the insider lists can be set up within the issuer, EAMP, auction platform, auctioneer, and auction monitor and presented to the relevant Competent Authority:

- A general list encompassing all insiders involved in the relevant projects of an issuer.
- A deal-specific list detailing the insiders in relation to a specific set of inside information.

There is also flexibility as to whether the issuer includes the insider lists of related third parties with their own insider list, or simply submits them as separate insider lists.

ESMA requires the insider lists to be submitted in the language of the relevant Competent Authority or a language customary in international finance. Furthermore, the lists must be in a secure electronic format which can be computer read and processed, although the exact format that must be used is not specified.

Maintaining and updating

The insider lists should be kept by the insider for a minimum period of five years since the last point of update. This means that when updates to the list take place, the previous insider list should not be overwritten, but rather a new version of the list should be created, such that the issuer keeps on record the content of the insider lists at different points in time. When circumstances change, the insider lists should be updated accordingly and without unnecessary delay. Relevant insider lists should be provided without delay on request by the Competent Authority.

Exemption for SME growth market issuers

Issuers on SME growth markets are exempt from creating, maintaining and updating a contemporaneous insider list under Article 18 of the MAR under the condition that they can provide an insider list upon request of the Competent Authority. In this respect, ESMA proposes that they are required to submit an insider list containing the appropriate information and in the proper format.

4.5.2 Technical standards – managers' transactions notification and disclosure

Individuals in management roles are likely to possess undisclosed, market-sensitive knowledge about the performance and strategic direction of their employer. Transactions based on such knowledge of inside information would constitute market abuse. Therefore, persons discharging managerial responsibilities (PDMRs) and those closely associated to them (closely associated persons) must notify their employer and the relevant Competent Authority of any transactions in financial instruments linked to their employer. Besides, this information should also be publicly disclosed. In the case of an issuer this encompasses trade in shares or debt instruments of that issuer, or derivatives and other financial instruments linked to these securities. And, in the case of an EAMP, auction platform, auctioneers, or auction monitor this includes transactions relating to emission allowances, as well as auctioned products and derivatives linked to emission allowances.

The obligation to notify and publicly disclose relevant transactions of PDMRs and closely associated persons already existed under MAD, but MAR has extended the scope of this obligation to cover financial instruments admitted to trading, those for which a request has been made to trade on a MTF, and those traded on an OTF. The MAR has also reduced the timeframe for notifying such transactions, from five days to three. As with the insider lists discussed above, ESMA's focus is on defining the specific format of such transaction notifications and publications.

Content

ESMA proposes a single template for notification comprising two sections; the first detailing on a transaction-by-transaction basis; and the second providing aggregated figures to be used for publication purpose. ESMA specifies that the following content must be included in the notification:

- Name of person or legal entity, address and contact details.
- The position occupied by the PDMR, and the relationship of the closely associated person for disclosure to the relevant Competent Authority only (not for public disclosure).
- National identification number.
- Details, as set out by MiFIR, on the following; the nature and identification number of the financial instrument; the transaction type; the price and volume; and the date and place of execution.

For aggregation, ESMA proposes that all transactions of a given financial instrument carried out on the same day are aggregated (though not netted), and the weighted average price, as well as the day-high and -low prices, reported.

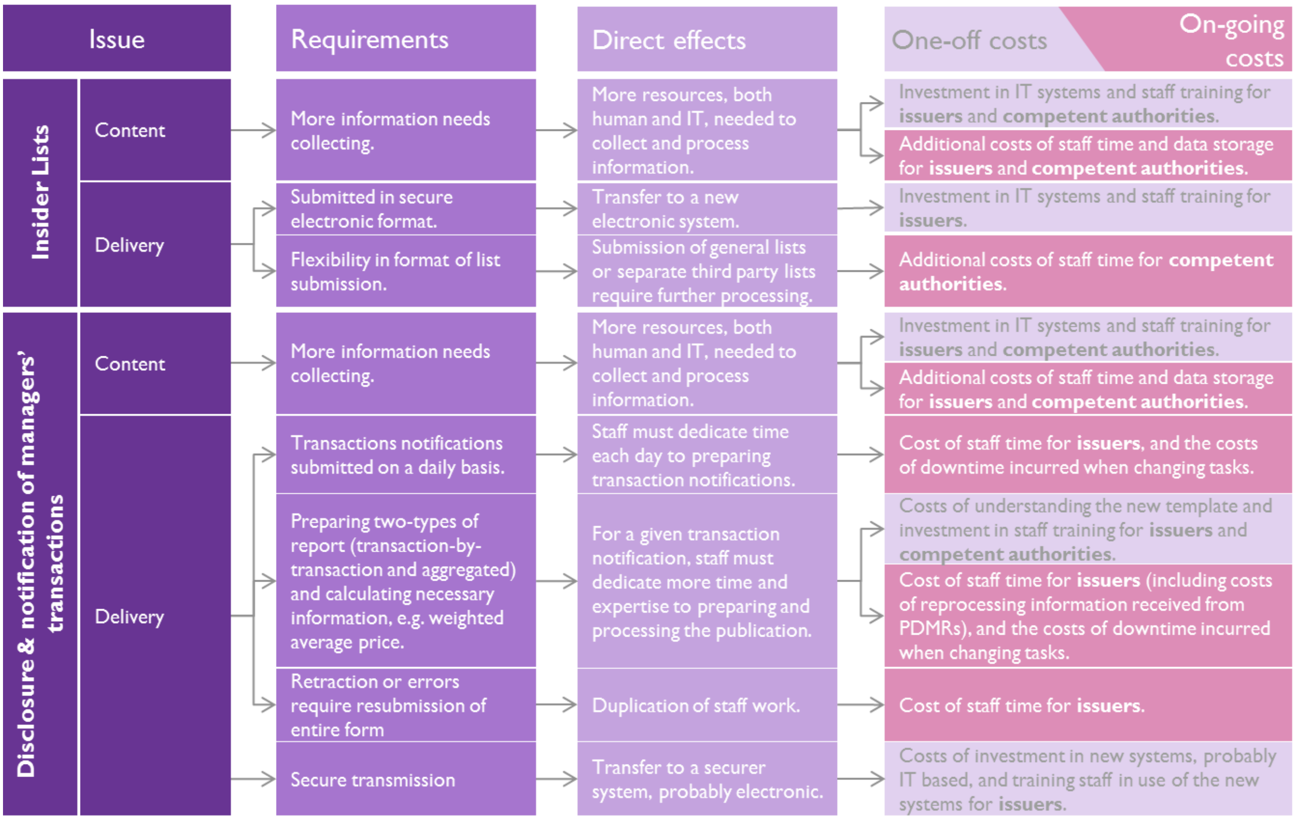
Delivery

With respect the delivery to the Competent Authority and the employer, ESMA proposes that whatever electronic form is used the safety and integrity of the information should not be placed at risk. If a notification needs to be retracted or corrected for errors, then an explanation of this should be provided by the relevant party and the entire notification resubmitted.

ESMA also specifies the channels for ensuring the publication of the aggregated information i.e. the ones to be used by issuers and EAMPs for disclosure of inside information, except when the Competent Authority ensures the publication.

4.5.3 Mechanisms of effect

Figure 4.8: Mechanisms of effect for format of insider lists and of transactions with managerial responsibility with an issuer



Source: Europe Economics.

4.5.4 Compliance costs and other impacts

Issuers and PDMRs

The costs imposed by the new standards on insider lists and the disclosure and notification of managers' transactions should include both one-off implementation costs and ongoing administrative costs.

The one-off implementation costs include the costs of understanding the standard and its requirements, which could include the employment of external professional services, such as consultancy and legal services, if competent in-house services are not available. A further upfront cost will be that incurred when migrating to, upgrading or adding additional IT systems infrastructure, both hardware and software. This may be necessary in order to increase capacity for recording and reporting additional information, and in order to establish a sufficiently secure electronic format for delivery to competent authorities. This could be significant for those issuers who currently use email or written submissions, and responses to ESMA's discussion paper suggest that these costs could be a particularly significant concern for small companies. Issuers will also then have to train staff in how to develop and use such systems. In addition, issuers would incur costs in adjusting their existing data collection process in order to obtain the extra information from insiders that would be required under ESMA's proposals. Responses to the discussion paper were generally of the view that any reduction in administrative burdens (thanks to a more harmonised system) could be offset by the volume of information that must be collected in accordance with ESMA's proposals.

Ongoing administrative costs will primarily comprise the cost of staff time, for those staff tasked with continually developing, reviewing and maintaining the insider lists and notifications of managers' transactions. This could be complemented, to a lesser extent, by the costs of maintaining IT systems and the costs of data storage.

Another ongoing cost is the cost of submitting the insider lists or managers' transactions notifications to the National Competent Authorities, which will largely constitute the opportunity cost of staff time in the preparation, certification and dissemination of the information. Leuz and Wysocki (2008)[37] argue that as these costs of reporting will be largely fixed, economies of scale imply that a disproportionately large burden could be placed on smaller firms. However, if the insider lists have been maintained properly in accordance with ESMA's other standards, then the marginal costs of submitting the insider lists to the relevant authority should be relatively small. In the case of the notification of managers' transactions two-types of report must be submitted, i.e. transaction-by-transaction and aggregated, which includes calculating weighted average price for the aggregated report. This will impose additional costs of staff time in processing information so that it is in an appropriate form for each report. Retraction or errors in transactions reporting require the resubmission of the entire form which will duplicate staff work and staff costs and, in order to reduce the likelihood of resubmission, this may encourage more thorough checking of forms ex ante which will itself incur additional staff costs. While this responsibility, strictly speaking falls on the PDMRs, we have taken the view that they will pass any compliance costs so incurred to their respective firms, i.e. PDMR resources are diverted from more productive tasks for the firm in order to meet these additional administrative requirements.

The general consensus emerging from our own stakeholder engagement, as well as the responses to ESMA's consultation paper, is that the amount of information required will create large administrative burdens. Stakeholders saw this as likely to be disproportionate to the potential benefit of this additional information. Many stakeholders feel that the additional data fields have little use in the identification of insiders and are thus an unnecessary cost. Some firms may have over 15,000 insiders over a year and this helps to understand how the additional data requirements could so dramatically be burdensome for such firms. These costs could be particularly inflated due to the practical difficulty of collection, as this is information which many stakeholders do not currently collect and which employees have no legal obligation to provide or may feel uncomfortable in providing. This could be further exacerbated for firms with an international reach, who must collect data from employees across a range of countries (and for their families in the context of PDMR templates/ notifications).

Stakeholders foresee high costs of initial data collection, but also significant costs in keeping the data up-to-date and secure. Several respondents said that a number of the pieces of information required by ESMA's draft Technical Standards are already stored in HR databases and, as such, it would be much less costly to make this available to Competent Authorities on request than to continually update this information on separate insider lists. Given that several pieces of relevant information are currently stored in HR databases, a small number of stakeholders recognised the need to significantly adapt the existing IT infrastructure to allow a direct feed of information from existing HR databases to insider lists. Although only mentioned by a small number of respondents, this seems to be the likely response of any stakeholders who currently store required information in separate internal HR databases.

Sell-side institutions

Sell-side institutions may also be affected by the technical standards in so far as sell-side employees may have access to the inside information of issuer clients who they support in an advisory role. Insider lists, and hence the cost of the technical standards, would therefore only be relevant in the case of sell-side institutions with issuer clients, and not to those sell-side institutions who are exclusively involved in order execution. The latter are unlikely to incur costs as the processing of orders is unlikely to yield inside

[37] Leuz, C. and Wysocki, P. (2008), 'Economic Consequences of Financial Reporting and Disclosure Regulation: A Review and Suggestions for Future Research', Working paper, University of Chicago and Massachusetts Institute of Technology.

information that require the maintenance of insider lists, as these orders are very quickly revealed to market. This rationale is reflected in the estimate of the affected sell-side population.

However an issue here is that the cost estimates we received from sell-side firms may have been 'contaminated' by considerations driven by the need of some of those sell-side firms maintaining insider lists because they themselves are issuers. This creates a potential issue of double-counting whereby the compliance costs for issuers, are also captured in the compliance costs for sell-side firms (who are themselves issuers). To mitigate this issue we adjusted the compliance costs reported by the sell-side institutions by the compliance costs reported by per non-financial issuers. We note that our analysis of the mechanisms of effect did not identify particular drivers of cost for the sell-side — this implies that even this adjustment may still leave the sell-side's reported costs over-stated.

For those sell-side institutions with issuer clients, the compliance costs of the technical standards on the format of insider are likely to be the similar to those faced by issuers, as described in detail in the previous section on 'issuers'. These similarities are indeed reflected by the survey and consultation responses of sell-side institutions.

The survey evidence suggests that the major one-off cost for sell-side institutions will be those associated with investing in new, or updating existing, IT infrastructure. This is consistent with qualitative stakeholder responses which identified the need to invest in IT systems to link up existing HR databases with the separate insider lists. The costs of understanding regulation and training relevant staff in the new regulation requirements are other key one-off costs, along with the costs of redeveloping the relevant list. The majority of sell-side firms, however, did not anticipate any costs for redesigning/increasing reporting to competent authorities or employing external professional services. This suggests that most sell-side institutions reporting capacity is sufficient to cope with the changes and that they, in the most part, have sufficient in-house expertise to adapt to the regulatory changes.

The survey and consultation responses identify two key ongoing costs as the costs of reviewing and maintaining the insider lists and the costs of maintaining the new IT structure. Firms are expecting to incur ongoing IT maintenance costs to ensure that the data stored on insider lists remains secure, particularly given the personal nature of the information. Furthermore, there is general agreement that, given the additional data fields required, as set out in L2, and given the large number of insiders to which this would apply, as set out in L1, the multiplicative impact of these two factors on the total resource costs of maintaining insider and PDMR templates/ notifications could be particularly significant and unduly burdensome.

The quantitative responses to the survey did suggest that sell-side institutions would incur compliance costs as a result of the technical standards concerning the format of PDMR notifications. However, we do not foresee that sell-side institutions can incur any compliance costs in this respect except in their role as an issuer. The technical standards apply only to individuals in management roles at issuers (including EAMPs). Therefore, we are of the view that the compliance costs reported by sell-side institutions are those incurred in their role as an issuer of securities.

Buy-side institutions

Employees of buy-side institutions could also be privy to inside information that would drive the organisation's own investment strategy and are, therefore, also covered by insider lists. However, in contrast to the sell-side, the buy-side firms surveyed identified no quantitative costs as a result of the new Technical Standards. This is in line with our expectations for this stakeholder group.

Trading venues

Trading venues are unlikely to face any direct compliance costs as a result of the regulation. This is reflected in our stakeholder engagement for which the four trading venues reported no compliance costs as a result of the regime, with the exception of one organisation who said that they would incur some very minor one-off costs in understanding the regulation and in training staff on the new regulatory requirements. However, that aside, no further compliance costs were envisaged. Overall, therefore, we expect no material costs to be incurred by trading venues as a result of the technical standards on either insider lists or PDMR templates/ notifications.

Quantitative compliance cost estimates

Table 4.17 to Table 4.20 show the one-off and ongoing per firm costs. Clearly, per firm costs for large sell-side institutions are significantly higher than for any other stakeholder group in the context of the format of insider lists. Nevertheless, these costs are trivial when compared with company operating expenditure and are, therefore, unlikely to have material impacts on market behaviour. Ongoing per firm costs for insider lists are fairly similar across the sell-side, the buy-side and issuers.

Table 4.17: Per firm one-off compliance costs for technical standards on the format of insider lists (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	146.6	191.0	21.5	28.0	2.2	2.8
Buy-side	12.9	17.4	1.9	2.6	0.2	0.3
Issuer	18.9	34.2	3.3	5.8	0.3	0.6
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

Table 4.18: Per firm annual ongoing compliance costs for technical standards on the format of insider lists (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	11.4	27.0	1.0	3.0	0.1	0.3
Buy-side	33.5	45.3	5.0	6.8	0.5	0.7
Issuer	32.2	43.8	5.6	7.6	0.6	0.8
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

The key cost driver of the above is the amount of personal information required to be collected. Our fieldwork indicated some minor ongoing costs associated with IT maintenance, but the majority of costs were attributed to the ongoing review and maintenance of the insider lists themselves. These costs (in particular the ongoing costs) would be strongly dependent upon the amount of personal information that these stakeholders are required to include in the insider lists.

The one-off and ongoing compliance costs associated with the format for PDMR notifications fall exclusively on issuers.

Table 4.19: Per firm one-off compliance costs for technical standards on the format of PDMR templates/ notifications (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	0.0	0.0	0.0	0.0	0.0	0.0
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	20.4	28.9	3.4	4.9	0.3	0.5
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

Table 4.20: Per firm annual ongoing compliance costs for technical standards on the format of PDMR templates/ notifications (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	0.0	0.0	0.0	0.0	0.0	0.0
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	1.1	1.4	0.2	0.2	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

In terms of the affected population, we assume that all buy-side firms and issuers are potentially affected by the new technical standards concerning the format of insider lists. Of the sell-side institutions, we assume that only those with issuer clients will be affected by the technical standards (see 4.4.3 above).

Based on these population estimates, Table 4.21 and Table 4.22below set out the total one-off and ongoing compliance costs for the technical standards on the format of insider lists.

Table 4.21: One-off compliance costs for technical standards on the format of insider lists (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	3.5	4.6	1.9	2.5	1.3	1.7	6.7	8.7
Buy-side	0.3	0.4	0.4	0.6	0.6	0.8	1.3	1.8
Issuer	4.7	8.5	6.3	11.0	2.0	3.5	13.0	23.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**8.6**	**13.6**	**8.6**	**14.1**	**3.8**	**5.9**	**21.0**	**33.5**

Source: Europe Economics estimates.

Table 4.22: Ongoing (annual) compliance costs for technical standards on the format of insider lists (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.3	0.6	0.1	0.3	0.1	0.2	0.4	1.1
Buy-side	0.8	1.1	1.1	1.5	1.5	2.0	3.4	4.7
Issuer	8.0	11.0	10.6	14.4	3.4	4.6	22.0	30.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**9.2**	**12.7**	**11.8**	**16.2**	**4.9**	**6.8**	**25.9**	**35.7**

Source: Europe Economics estimates.

The estimates in Table 4.21 and Table 4.22 show that the total compliance costs for the technical standards relating to the format of insider lists will fall principally on issuers and sell-side institutions, and in particular issuers in terms of ongoing compliance costs. Despite the higher per firm costs for sell-side institutions, the significantly larger population of issuers means that a higher proportion of the total compliance costs falls on issuers.

For buy-side institutions and issuers the annual ongoing compliance costs are in excess of the one-off compliance costs and this is largely a reflection of the high costs of reviewing and maintaining insider lists on an ongoing basis. However, for sell-side institutions the one-off cost is well in excess of the estimated annual ongoing costs which is principally attributable to the high anticipated costs of investing in IT systems infrastructure or upgrading existing IT infrastructure, which the majority of surveyed sell-side institutions deemed to be necessary.

With regard to the format for PDMR notifications, we assume that the whole population of issuers would be affected. No other stakeholder groups would be.

Table 4.23: One-off compliance costs for technical standards on the format of PDMR templates/ notifications (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	5.1	7.2	6.5	9.2	2.1	2.9	13.7	19.4
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**5.1**	**7.2**	**6.5**	**9.2**	**2.1**	**2.9**	**13.7**	**19.4**

Source: Europe Economics estimates.

Table 4.24: Ongoing (annual) compliance costs for technical standards on the format of PDMR templates/ notifications (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.3	0.4	0.3	0.4	0.1	0.1	0.7	0.9
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**0.3**	**0.4**	**0.3**	**0.4**	**0.1**	**0.1**	**0.7**	**0.9**

Source: Europe Economics estimates.

Table 4.23 and Table 4.24 show the compliance cost estimates for the technical standards relating to PDMR. The compliance costs are solely attributable to issuers. On a one-off basis these compliance costs are of a similar magnitude to the compliance costs associated with the format of insider lists, but on an ongoing basis the compliance costs are significantly lower. The survey responses from issuers attribute this too much higher ongoing costs of maintaining and reviewing the insider lists and maintaining the IT systems that underpin this.

Competent authorities

Although the costs to competent authorities have not been considered as part of the survey or earlier consultation responses, we briefly set out the potential impacts on this stakeholder group. The costs can be considered in terms of one-off implementation costs and ongoing costs.

The one-off costs are likely to include the cost of training staff in understanding and using the new insider lists and managers' transaction notifications as well as the costs of upgrading or investing in new IT systems to process and store the additional information.

The ongoing administrative costs will largely be attributed to the cost of staff time dedicated to receiving and processing the incoming information. As with issuers, there may also be small IT maintenance and data storage costs. Furthermore, ESMA's proposal to allow separate submission of insider lists by the issuer and related third parties may impose an additional ongoing administrative burden on competent authorities, who may incur additional staff costs in merging the lists so that a breakdown of insiders can be given by each piece of inside information.

Overall, as competent authorities are not responsible for actually producing insider lists, we envisage that the costs to competent authorities will be significantly less than sell-side firms or issuers, and are unlikely to be anything but negligible.

Other adverse market impacts

The key wider implication, which was brought to attention by several respondents of both our fieldwork and the initial consultation paper, is the potential conflict between ESMA's draft Technical Standards and existing data protection laws, specifically European Directive 95/46/EC, or the Data Protection Directive. This mandates that the collection of personal data must be "adequate, relevant and not excessive in relation to the purposes for which they are collected and/or further processed". This is relevant to records like home and personal mobile telephone numbers, home address, personal e-mail address and birth surname. Therefore, if this concern is valid, the obligation to collect these under ESMA's draft Technical Standards could put stakeholders at risk of non-compliance with data protection regulation.

Even if not deemed in breach of existing data protection legislation, the majority of stakeholders still saw the L2 standards as overly intrusive of personal privacy given their purpose. Stakeholders from all categories deemed many of the personal information requirements set out in the draft technical standards as redundant in identifying PDMRs. The requirements are seen as particularly in invasive in the case of providing information on closely related persons, i.e. the immediate family, for those in managerial roles. One respondent said that this could go as far as detracting existing managers from the industry.

Some of the consultations responses also said that the technical standards would lead to greater risk of fraud or personal identity theft. This could itself fuel a reluctance to provide personal contact information.

Many organisations spoke of how the fields of data required were excessive given the aim of identifying insiders and PDMRs, namely home and personal mobile telephone numbers, personal e-mail address and home address. The general view is that such requirements would introduce operational inefficiencies with no commensurate benefit to preventing market abuse.

These issues relating to personal privacy were the key wider impacts discussed in both our survey and the consultation responses. Aside from this, one respondent spoke of how the additional information requirements could increase the risks of mistakes and hence violation of the Market Abuse Regulation. And as violations against Article 13 of MAR could lead to fines of €500,000-€1,000,000 the risk of non-compliance may be sufficient to decrease the attractiveness of organised capital markets as a source of finance, particularly for smaller issuers for whom it would represent a larger risk.

This could, in extreme cases, cause a prospective issuer to choose not to list on a trading venue and thereby reduce the potential listing fees received by trading venues. We do not consider this to be practicably plausible, as this is likely to be only a small driver of an owner's or management team's decision of whether, or not, to list and, as such, we expect no material impact on listing decisions.

4.6 Objective presentation and disclosure of conflicts of interest

This set of technical standards concerns objectivity in conducting and presenting investment recommendations, and the disclosure of conflicts when doing so. Failure to meet these standards would constitute market abuse. The MAR does not make significant changes to the approach of the MAD. Therefore, in developing draft technical standards mandated by Article 20(3) of MAR, ESMA is of the view that the current measures in place under MAD are a sound base from which to further develop these standards.

4.6.1 Technical standards

There are five key areas in which ESMA has developed technical standards:

- regulatory scope;
- date and time of disseminations;

- production of recommendations (including identity of producers, objective presentation and disclosure of interests and conflicts of interest);
- non-written recommendations; and
- dissemination of recommendations by third parties.

The technical standards developed by ESMA in each area are looked at in turn.

Regulatory scope

ESMA develops a two-tiered approach, in line with the MAR Level 1 and the existing MAD, as follows:

- General obligations applying to all 'qualified' and 'non-qualified' persons, as defined by MAR Article 3(1)(34).
- Additional obligations applying to all 'qualified' persons, as well as any 'non-qualified' persons considered 'experts', where an 'expert' is defined as someone who repeatedly proposes investment decisions, and either sees himself as possessing financial expertise or experience, or produces recommendations in a way that suggests financial expertise or experience.

Any note that falls under the MAR definition of 'investment recommendations' (Article 3(1)(35)) or 'information recommending or suggesting an investment strategy' (Article 3(1)(34)) is subject to the technical standards. This includes all investment recommendations intended, or expected, to be publicly available, as well as non-personal recommendations delivered to one (or more) clients. However, ESMA does not propose setting a quantitative threshold with regard to what constitutes a 'large number of persons' to further specify public availability.

Date and time of disseminations

Investment recommendations must include the date and time at which the recommendation was first released for distribution.

Production of recommendations

Identity of producers – the technical standards state that all investment recommendations must disclose the name and job title of the person responsible for its production, as well as the name of the person responsible from a legal standpoint. This only applies when the individual is acting in his capacity as an employee. Furthermore, in the case of an investment firm or credit institution or where individual operates under self-regulatory standards, then the disclosure must identify the relevant Competent Authority or self-regulatory standards respectively.

Objective presentation – ESMA applies its two-tiered approach to the standards of objective presentation. These standards are based on those currently in use under MAD.

General standards, applicable to all persons defined under MAR Articles 3(1)(34)(i) and 3(1)(34)(ii), include that; facts and opinions are clearly differentiated; underlying assumptions are presented and projections they generate clearly marked; and reliable sources are used wherever possible and any potential lack of reliability flagged.

ESMA proposes a list of additional standards, applicable to qualified persons defined in Article 3(1)(34)(i) and experts within Article 3(1)(34)(ii), which must include; the valuation or methodology involved in setting a price target, in summary form; the frequency with which the recommendation will be updated, if at all; and any change in recommendation relative to the last relevant recommendation, including the date of this prior recommendation (providing it is in the previous 12 months). A further obligation for qualified persons and experts is to keep a list of all recommendations made in the preceding year with information on: producer identity, release date, direction of recommendation, market price, target price and period of validity for the recommendation. In terms of disclosing methodologies and assumptions, it is only necessary to do so in the recommendation itself if the methodology or assumptions have changed; otherwise an indication in the recommendation of where such information can be found will suffice. ESMA also encourages methodological consistency for recommendations on related companies/industries. However, when the recommendation is based on a proprietary model, the methodological details of such model may not be disclosed, only the key factors underpinning it and the extent to which its results mark a departure from existing models.

Disclosure of interests and conflicts of interest — ESMA also applies a two-tiered approach to the requirements regarding disclosure of interests and conflicts of interest, adopting the same technical standards as those in the MAD and complementing them. The disclaimers themselves should be clear, accurate and complete and include an indication of the risk of acting on investment recommendations with delay, as the trading position could become outdated.

The general standard (derived from Article 5 of the Implementing Directive 2003/125/EC) mandates the disclosure of any relationship or circumstance — in particular investment in financial instruments which are subject of the recommendation — that may call in to question the objectivity of the investment recommendation. This applies to any person involved, either directly or indirectly, in the production of the recommendation, or else anyone who could feasibly have accessed the recommendation prior to its public dissemination.

The additional obligations (derived from Article 6 of the Implementing Directive 2003/125/EC) for qualified persons and experts are to disclose significant shareholdings and financial interests in any issuer subject of a recommendation, as well as details of the activities engaged in and agreements made with the issuer regarding the recommendation. ESMA proposes that significant shareholdings are defined as holdings in excess of 0.5 per cent of the total issue, which will apply to both long and short positions held in the company. This compares to the current disclosure requirement for shareholdings in excess of 5 per cent of the total issued share capital for long positions only. However, in the case that reference is made to specific financial instruments in the recommendation, then no threshold applies and all holdings in these financial instruments must be disclosed.

There are also further disclosure requirements on credit institutions and investment firms including details on the administrative and organisational structure in place to limit conflicts of interest arising, and whether individuals involved in the recommendation purchased or sold shares in the relevant issuer prior to the public offering of those shares. These firms must also disclose, on a quarterly basis, the proportion of buy, hold and sell recommendations and the proportion of issuers applicable to each.

Non-written recommendations

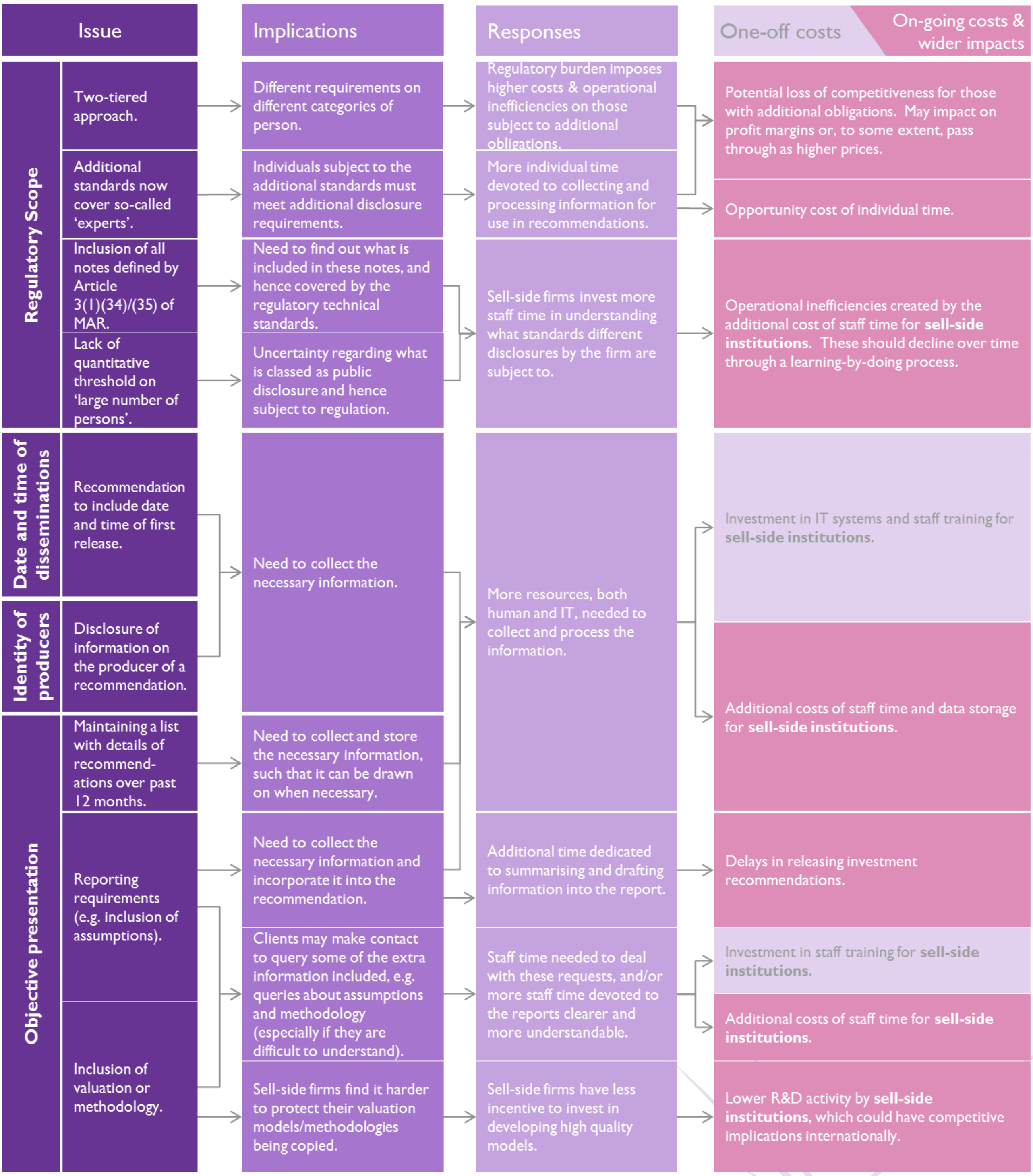
ESMA provides a non-exhaustive list of the modes that non-written recommendations encapsulate, e.g. road shows, radio and TV. The two-tiered objective presentation requirements apply in the same way as for written recommendations and, where relevant, the audience should be made aware of any supporting written recommendations that disclose conflicts of interest in full.

Dissemination of recommendations by third parties

The proposal is that the existing standards under MAD are to apply under the new regime. This states that where significant alterations are made to a third party recommendation, details of such changes should be flagged, and further details given if these changes result in a change in target price or direction of recommendation. The new recommendation should reference the original, as well as providing information with regard to where the disclosures of the original recommendation can be found. Furthermore, intermediaries that disseminate third party recommendations must disclose any relevant interests in accordance with the standards of Article 6 discussed earlier. Disseminating persons are excluded if they belong to the same group as the producer of the recommendation and their role purely concerns transmission and not production.

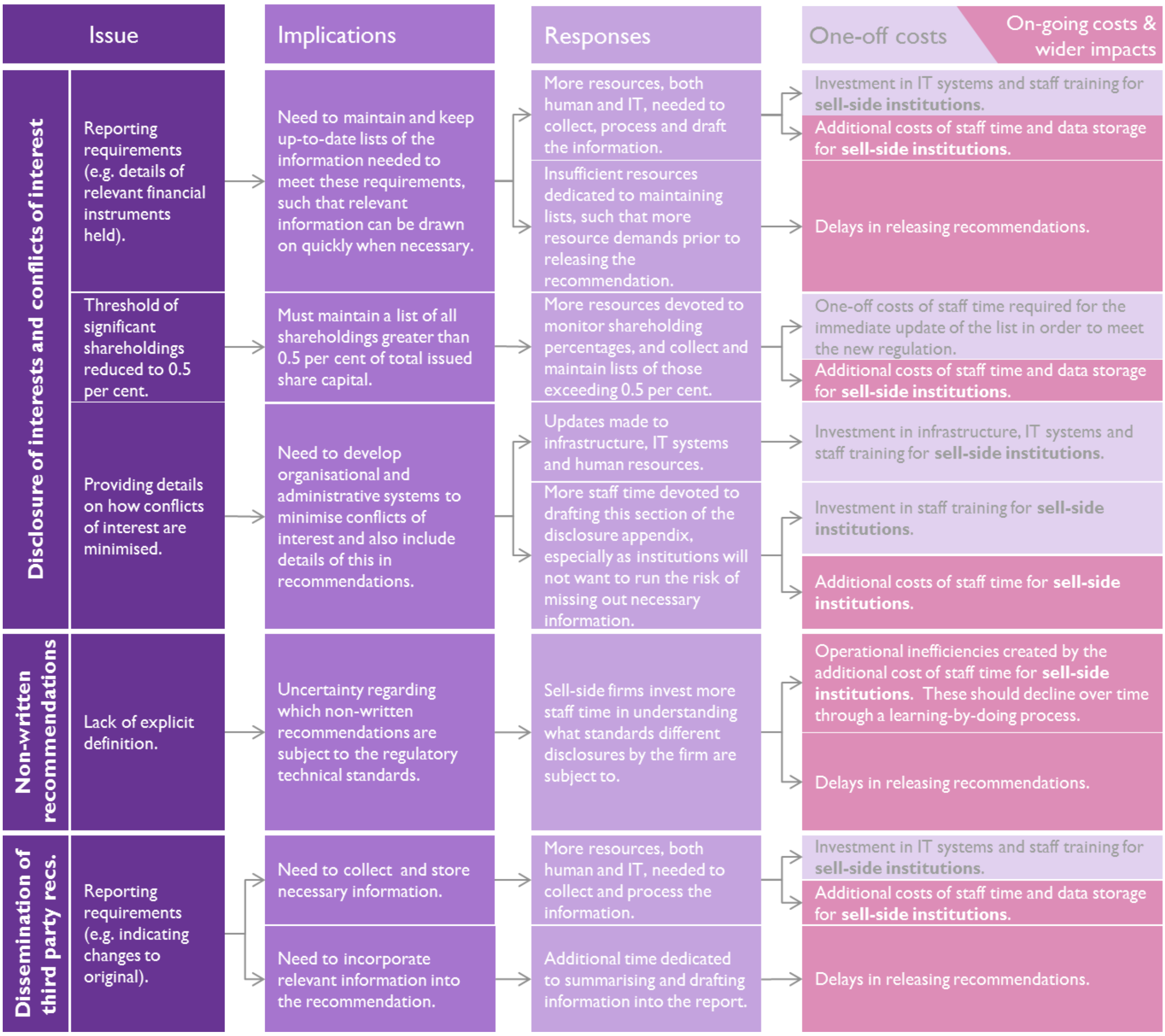
4.6.2 Mechanisms of effect

Figure 4.9: Mechanisms of effect for objective presentation and disclosure of conflicts of interest



Source: Europe Economics.

Figure 4.10: Mechanisms of effect for objective presentation and disclosure of conflicts of interest (cont.)



Source: Europe Economics.

4.6.3 Compliance costs and other impacts

Compliance costs

The mechanisms of effect outline the potential compliance costs that could arise as a result of the draft technical standards relating to objective presentation and the disclosure of conflicts of interest.

Sell-side institutions

The changes will generate some one-off adjustment costs for sell-side institutions and investors. As with the other Technical Standards, firms will incur the costs of understanding the standard and its requirements, which may include not only the cost of employees' time but also the cost of employing relevant external professional services. This may be particularly significant for smaller sell-side institutions who lack appropriate professional services in-house. New informational requirements may require investments to upgrade existing, or develop additional, IT systems or to migrate to new hardware and software. One-off costs are also likely to comprise the costs of training staff in how to meet the new regulatory standards, in how to use the new IT systems, and in how to draft the disclosure sections of recommendations (in order to minimise the likelihood that the new disclosure requirements are not met).

Larger one-off costs may be imposed on those firms who do not currently have sufficient administrative and organisational structures in place to limit the opportunity of conflicts of interest arising. Credit institutions and investment firms, who must disclose information on such structures in the annex of their investment recommendations, may choose to redevelop existing structures if they expect that their current structures will not be perceived as satisfactory. By its own admission, ESMA expects that the downward revision of the 'significant shareholding' threshold from 5 per cent to 0.5 per cent could create significant administrative burdens. A portion of this will be the one-off costs on investors of updating their current 'significant shareholding' lists to respect the new regulation (the ongoing costs of this are discussed below).

Sell-side institutions should also incur the costs of ongoing administrative burdens created by the new disclosure requirements. The standards which mandate the disclosure of the date and time of dissemination and the identity of producer should be relatively less resource intensive, as the former is a very straightforward and quick task and the latter is likely to be information stored by the company already. However, the new reporting requirements relating to objective presentation and the disclosure of interests and conflicts of interest could impose much greater compliance costs. This includes compiling additional detail both on the investment recommendation process itself, e.g. the valuation models used, and on other disclosure requirements, e.g. past recommendations. The additional information required could take significantly longer to collect and process, and then draft in an appropriate manner for inclusion in the final recommendation. This implies a higher requirement of staffing hours and therefore an increase in staff costs; costs which could be exacerbated if additional staff must be hired and/or trained to fulfil these commitments.

The obligation to report on the organisational and administrative systems in place to minimise conflicts of interest could be particularly consuming of staff time, especially as firms are unlikely to want to run the risk of failing to include what the authorities deem as relevant information. Data storage and IT maintenance costs could also increase with new reporting requirements, although the human resource costs should constitute the bulk of additional costs. Perhaps the largest impact on sell-side firm's administrative burdens, as touched on earlier, is the lower 'significant shareholding' threshold. The implication is that investors will have to devote more time to monitoring shareholdings and updating their lists of significant shareholdings, such that the relevant information can be easily accessed for inclusion in investment recommendations.

An overarching issue is the scope of the new technical standards. The key change in this regard is that, although ESMA proposes a twofold approach in line with the existing MAD, they also propose that the additional obligations will apply not only to 'qualified persons' but also to those classed as 'experts' (see earlier definition). Under MAD, these individuals are only subject to the general standards, so ESMA's proposals will mark a significant change for this classification of persons, with all additional obligations imposing new costs on this group. However, for those individuals who remain subject to the same obligations, either 'general' or 'additional', the incremental costs are likely to be smaller and primarily the result of providing additional information that is not requested in the current MAD regime.

The key one-off compliance costs reported by sell-side institutions in the survey were: understanding the new regulation; training staff; adjusting the investment recommendation and disclosure formats/processes in light of the additional detail required; and redesigning, and/or increasing, capacity to report to competent authorities. Although of similar magnitude, the most significant one-off cost is the cost of training staff in the new regulation. This seems highly plausible given that the key firm-level response will be to ensure that employees who produce the investment recommendations understand the new reporting requirements that must be adhered to. No supply-side firms see it as necessary to invest in new, or update existing, IT infrastructure, revise the firm's organisational structure or employ external professional services.

The ongoing costs are expected to be very small and exclusively driven by the need to compile additional detail on additional disclosures and for investment recommendations. The former could, to a large extent, relate to the reduced significant shareholdings threshold from 5 per cent to 0.5 per cent. However, that said, stakeholders responses suggest that these ongoing costs will not be material.

Buy-side institutions and brokers

We do not anticipate any cost for buy-side institutions as a result of these technical standards relating to objective presentation and disclosure of conflicts of interest. This is supported by the survey responses of buy-side firms who reported no compliance costs. This regulation is not applicable to buy-side firms as research remains in-house and, therefore, is not subject to the traditional disclosure requirements of sell-side research.

Issuers

As can be seen from the mechanisms of effect diagrams in 4.6.2, we do not anticipate any compliance costs for issuers, as they do not engage in the production or dissemination of investment recommendations.

The survey responses suggested some minor compliance costs for issuers, specifically one-off costs of understanding the regulation and in training staff accordingly. However, we do not believe there to be a plausible mechanism by which such costs for arise for issuers. Therefore, it is our expectation that issuers would not incur compliance costs in any systematic way.

Trading venues

There are no foreseeable impacts on trading venues, and this is supported by evidence from the survey in which no trading venue identified any compliance costs.

Quantitative compliance cost estimates

The one-off and ongoing per firm costs are set out in Table 4.25 and Table 4.26 below. It shows that the only sell-side firms incur costs, both on a one-off and ongoing basis. Once again, however, these compliance costs lack materiality when considered as a proportion of total operating expenditure and so the impact of these costs on firm behaviour and the wider market should be limited.

Table 4.25: Per firm one-off compliance costs for technical standards on objective presentation and the disclosure of conflicts of interest (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	81.7	110.6	12.3	16.6	1.6	2.2
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.0	0.0	0.0	0.0	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

Table 4.26: Per firm annual ongoing compliance costs for technical standards on objective presentation and the disclosure of conflicts of interest lists (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	13.4	18.1	2.0	2.7	0.3	0.4
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.0	0.0	0.0	0.0	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0

Source: Europe Economics estimates.

In terms of estimating the relevant population, we assume that the affected sell-side population would be limited to the sell-side players who produce and disseminate research. Our estimate is that all sell-side institutions classed as large or medium would do so, but that the smaller firms would be unlikely to engage in such activity and, as such, we exclude them from the relevant population.

Estimating the relevant populations for the buy-side, issuers and trading venues is unnecessary as these stakeholder groups would incur no costs as a result of the proposed technical standards.

Table 4.27 and Table 4.28 below show the one-off and ongoing compliance costs respectively.

Table 4.27: One-off compliance costs for technical standards on objective presentation and the disclosure of conflicts of interest (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	2.0	2.7	1.1	1.5	0.0	0.0	3.1	4.1
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**2.0**	**2.7**	**1.1**	**1.5**	**0.0**	**0.0**	**3.1**	**4.1**

Source: Europe Economics estimates.

Table 4.28: Annual ongoing compliance costs for technical standards on objective presentation and the disclosure of conflicts of interest (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Sell-side	0.3	0.4	0.2	0.2	0.0	0.0	0.5	0.7
Buy-side	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Issuer	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Trading	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	**0.3**	**0.4**	**0.2**	**0.2**	**0.0**	**0.0**	**0.5**	**0.7**

Source: Europe Economics estimates.

The large sell-side institutions are likely to incur the majority of the costs (as shown in Table 4.25 and Table 4.26), both one-off and ongoing, as together they will produce a very high proportion of all investment recommendations.

Competent authorities

Competent authorities are unlikely to incur further costs as a result of these technical standards.

Other adverse market impacts

The extent to which sell-side institutions and investors adapt their current operations in light of the new technical standards could affect the degree to which indirect costs and wider impacts may arise. Failure to keep relevant information up-to-date and easily accessible could lead to delays in the dissemination of investment recommendations or opinions that, from an investor's standpoint, are ready for public release.

Our fieldwork produced mixed results, with some respondents believing that the reporting requirements could lead to delays, while others did not. Interestingly, the large sell-side respondents who commented on this did not expect delays to the dissemination of investment recommendations, with one respondent saying that it would not require significant changes to the approach used under MAD. That said, a respondent to the consultation paper said that normal communications between investment firms and issuers would be materially impeded, if every time they approached a client they were required to send the full range of information relating to objectivity and conflicts of interest. They further believe that this obstacle to the flow of investment information could hamper liquidity in some investment, and in particular in SME shares. However, this liquidity concern was not raised by any other respondents.

Another indirect cost that could arise is the cost of responding to client queries relating to the new disclosure requirements, such as the underlying assumptions and valuation models. The disclosure of extra information may raise new questions for clients that the sell-side institutions then need to respond to. This may be particularly pertinent when the underlying assumptions or valuations are more technical or quantitatively difficult, such that prospective investors have difficulty interpreting them without further clarification. Firms may respond by a combination of direct contact with clients and by investing more time in the initial recommendation drafting process to articulate technical ideas in a more investor friendly style. Both of these processes would impose extra staffing costs on sell-side firms.

Although there is some belief among stakeholders that the additional reporting requirements are lengthy and disproportionate and may detract from the overall clarity of the report, no stakeholders raised concerns about an increase in client queries as a result of the proposed technical standards.

A more serious concern may be the potential harm to research activity as a result of the requirements to disclose details on the valuation and methodology underpinning the investment recommendation. Sell-side firms will be wary of their intellectual property being copied by other institutions once their recommendations are publicly available. This threat of replication will reduce a sell-side institution's perceptions about the expected 'monopoly' profits it could earn from an innovative valuation model and, thereby, reduce the incentive to carry out the work that helps develop such models. Although the reporting requirements for proprietary models are rolled back to some degree, it is nevertheless the change in a firm's perceptions which is likely to be key to the impact on innovation. This detrimental impact on innovation could also cause sell-side institutions' international competitiveness to suffer. It could also be of detriment to investors by reducing the number of differing opinions on the market. However, this effect may be limited to the extent that valuation approaches that deviate substantially from accepted ways are more likely to be pioneered in academia, than sell-side institutions themselves. As such, the impact of disclosure requirements in valuation models may be rather limited.

The majority view among stakeholders, with regard to the above, is that innovation and the willingness to develop new valuation approaches will not be affected. A large sell-side firm justified this with the fact that their analysts already disclose their valuation models in this way and, therefore, no incremental impact. In addition, one issuer said that transparency of valuation models is a positive thing, because it can help to shed light on so far unfounded outcomes.

There are some aspects of the technical standards that create uncertainty and could, therefore, increase non-productive search costs and ultimately operational inefficiencies. This includes the lack of definition concerning non-written definitions and the lack of a quantitative threshold for what constitutes a 'large number of persons'. This uncertainty could increase search costs for sell-side firms and introduce delays to the dissemination of recommendations, as firms spend time researching what standards must be met. Search costs will consist of both external costs, which include the direct costs of acquiring the relevant new information and the opportunity cost of staff time dedicated to this, and internal costs, which are the costs of processing the information acquired and determining an appropriate course of action.[38] These costs, and the associated delays, could be exacerbated by a tendency to be overcautious in approaching a new regulatory regime, whereby producers include lots of extra details in the recommendations so as to minimise the risk that necessary information is excluded. However, these search costs and delays should decrease over time through learning-by-doing. Aside from search costs, a lack of clear definitions could also create opportunities for regulatory arbitrage and thereby dampen the intended impacts of the

[38] Smith, G. E., Venkatraman, M. P. and Dholakia, R. R. (1999), "Diagnosing the search cost effect: Waiting time and the moderating impact of prior category knowledge", *Journal of Economic Psychology*, vol. 20(3), p285-314.

Technical Standard. However, no stakeholders raised the lack of an explicit quantitative threshold for 'a large number of persons' as a significant concern.

4.7 Summary of costs

The tables below present the one-off costs per technical standard and total costs. Overall, we estimate that ESMA's proposed technical standards would cost stakeholders between €124m and €207m in one-off costs. We note, however, that in some places stakeholders had difficulty in separating L2 impacts from L1 impacts. We have tried to note this qualitatively and, where justifiable, attempt to isolate just the L2 impacts. Nonetheless, it is likely that there is some element of L1 cost embedded in these figures. Therefore, this range (and also the range for annual ongoing costs) should be viewed as potentially over-stating the true range for the L2 MAR technical standards.

Technical standards on disclosure and delays to disclosure of insider information are the largest single cost driver, followed by STORs, PDMR templates/ notifications, and insider lists. These are the most costly technical standards not necessarily because they are the most costly on a per firm basis but because the impacted population is relatively large, sometimes comprising the universe of firms in Europe. On a per firm basis, the most costly technical standards are those on STORs, PDMR templates/ notifications, and market soundings. Standards relating to buy-backs and stabilisations, market soundings, and disclosures in investment research are relatively small contributors, but the impacted population is also rather small.

Table 4.29: Per firm one-off compliance costs for all technical standards (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	795.2	1,131.2	117.6	166.3	9.2	12.2
Buy-side	24.7	33.2	3.7	5.0	0.4	0.5
Issuer	123.6	219.3	21.3	37.8	2.0	3.5
Trading	73.2	99.0	11.0	14.8	1.1	1.5

Source: Europe Economics estimates.

Table 4.30: One-off compliance costs for all technical standards (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Buy backs	2.5	3.5	1.5	2.1	0.0	0.0	**4.0**	**5.6**
Market soundings	5.7	9.5	3.5	5.7	0.1	0.1	**9.3**	**15.3**
STORs	7.4	10.4	3.5	4.9	18.8	26.9	**29.7**	**42.2**
Inside information	16.8	33.0	19.9	40.3	6.7	13.1	**43.4**	**86.4**
Insider lists	8.6	13.6	8.6	14.1	3.8	5.9	**21.0**	**33.5**
PDMR	5.1	7.2	6.5	9.2	2.1	2.9	**13.7**	**19.4**
Conflicts of interest	2.0	2.7	1.1	1.5	0.0	0.0	**3.1**	**4.1**
Total	**48.0**	**79.9**	**44.5**	**77.8**	**31.6**	**49.0**	**124.1**	**206.7**

Source: Europe Economics estimates.

The tables below contain the annual ongoing costs, again by technical standard and in total. According to our estimates, annual ongoing costs across all technical standards could be in the range of €55m to €84m. Here, technical standards on insider lists, STORs, disclosure and delays to the disclosure of inside information, and market soundings are the most costly standards. These are all standards that require information, scripts, or templates to be updated frequently and hence the higher ongoing costs. On a per firm basis, STORs stands out as the most costly, driven in large part by reporting requirements, storage of relevant records, and investment in IT infrastructure. This is followed by technical standards on insider lists, which require frequent updating of information, and market soundings, which generates ongoing storage and script maintenance costs.

Table 4.31: Per firm ongoing compliance costs for all technical standards (€000s)

	Large		Medium		Small	
	Low	High	Low	High	Low	High
Sell-side	179.1	278.7	25.9	40.3	2.2	3.3
Buy-side	33.9	45.8	5.1	6.9	0.5	0.7
Issuer	86.9	128.2	15.1	22.3	1.0	1.5
Trading	57.9	78.3	8.7	11.7	0.9	1.2

Source: Europe Economics estimates.

Table 4.32: Annual ongoing compliance costs for all technical standards (€m)

	Large		Medium		Small		Total	
	Low	High	Low	High	Low	High	Low	High
Buy backs	0.2	0.3	0.1	0.2	0.0	0.0	**0.3**	**0.5**
Market soundings	3.6	5.3	2.7	3.9	0.0	0.0	**6.4**	**9.3**
STORs	4.1	5.7	1.7	2.5	8.7	12.4	**14.5**	**20.6**
Inside information	2.7	6.3	3.1	7.7	1.0	2.4	**6.8**	**16.5**
Insider lists	9.2	12.7	11.8	16.2	4.9	6.8	**25.9**	**35.7**
PDMR	0.3	0.4	0.3	0.4	0.1	0.1	**0.7**	**0.9**
Conflicts of interest	0.3	0.4	0.2	0.2	0.0	0.0	**0.5**	**0.7**
Total	20.3	31.2	20.0	31.2	14.7	21.8	55.0	84.2

Source: Europe Economics estimates.

In the context of the operational scale of the affected firms, the direct compliance costs attributable to the technical standards are not large. This is reflected in the 'per firm' costs, shown in Table 4.29 and Table 4.31.

More importantly, according to the stakeholders participating in our fieldwork, are the potential adverse wider impacts. In particular there are concerns around the adverse impact on pre-transaction information gathering from market soundings and on the privacy and feasibility concerns of insider lists and PDMRs. These are expected to have consequences for current market practices greater than those implied by the directly identifiable compliance cost impacts, without providing significant benefits to market participants or other stakeholders.

Appendices

Europe Economics

5 Appendix — Sample and Calculation Rules

5.1 Data gathering methods

Data was collected through a combination of interviews and questionnaire responses, which collectively formed the stakeholder survey. This survey covered four key industry stakeholders: the sell-side; the buy-side; issuers; and trading venues. Competent authorities were not covered by the survey although their potential costs are assessed qualitatively in the main report.

The questionnaire document, provided in a separate annex, formed the basis for the interviews, as well the questionnaire itself. The questionnaire was divided into two sections, the first of which consisted of firm profiling questions and the second of which discussed the compliance costs and wider impacts of each of the technical standards in turn.

5.2 Sample description

Table 4.33 presents the target and achieved sample for this study, contacted using the research tools described above. In each case, we met or exceeded our sample target. Originally, we sought to separate sell-side firms and non-bank brokers. We faced difficulties in reaching non-bank brokers and, with the consent of ESMA, decided to substitute more sell-side firms for non-bank brokers. Where this was done we tried, where feasible, to focus on the brokerage operations of those banks.

Table 4.33: Target and achieved sample by stakeholder group

Group	Target	Achieved
Trading venue	3-4	5
Sell-side / brokers	5-7	7
Buy-side	2	2
Issuers	4+	8
Total	14-17	22

In addition as part of the stakeholder engagement process, we arranged a presentation to members of the European Federation of Energy Traders (EFET) at Gazprom's London office. The aim of this was to clarify ESMA's Technical Standards with the members and to encourage questionnaire responses from EAMPs.

5.3 Decision rules and cost modelling

5.3.1 Treatment of "Yes", "No", and "Maybe"

Respondents were asked to identify which cost drivers (e.g. training) were relevant to a particular Technical Standard as a precursor to being asked to quantify that cost impact. The following are the 'key' decision rules we used in interpreting the qualitative part of the survey evidence:

- A "yes" was treated as indication of a measurable cost, either one-off or ongoing.

- A "no" was treated as no measurable cost, on either a one-off or ongoing basis.
- A "maybe", in absence of supporting quantification, was also treated as no measurable cost (i.e. assumed negligible impact).

5.3.2 Quantification of one-off and ongoing costs

Where quantification was provided by the stakeholder, we incorporated this in the stakeholder analysis, unless there was very strong reasons to believe that the estimate provided was biased. Where firms did indicate a measurable cost, by ticking "yes", but did not provide quantification we have, where possible, imputed cost estimates using quantifications: based on the respondent's qualitative descriptions, drawing on estimates from other studies (e.g. around the cost of training), provided by other stakeholders — and adjusting the costs where necessary to take account of firm differences.

Where firms provided quantification in terms of man hours, number of full time equivalents (FTEs), etc. we adjusted these time requirements into monetary costs using estimated industry wage costs. As part of this we assumed a different set of wage costs for financial sector firms (sell-side, buy-side and trading venues) vis-à-vis non-financial corporate issuers. We also assumed different wage costs for compliance, IT and other (e.g. client facing) staff. This allows us to more accurately monetise any resource requirements denominated by time. Our assumptions on staff cost were as follows:

- Compliance workers: €60–80,000 per annum.
- IT workers: €80–100,000 per annum.
- Other client-facing staff: €80–100,000 per annum

An overhead multiplier of 1.5 was then applied.

Our upper and lower bound estimates of compliance costs are based on a ±15 per cent band. All the costs provided were converted into EURO prior to cost analysis using the average exchange rate from January 2014 to October 2014.[39]

This same approach was used for one-off and ongoing cost quantification. Where necessary we also used the ratio of one-off to ongoing costs, to help impute ongoing cost estimates where only one-off cost data had been provided. This meant that if one firm did not provide quantification of the ongoing cost, we could impute this by applying the ratio of another firm to the one-off cost of the firm in question. However, caution must be taken in applying this method more broadly because of differences in the fixed to variable cost ratios for different size firms.

5.3.3 Population and cost scaling

Our total population estimates for the key stakeholder groups are set out in in the main report. This section provides our estimation of the total EU population for sell-side firms, buy-side firms, issuers and trading venues. However, the precise population used for scaling the per firm compliance costs varies across the technical standards.

Per firm compliance cost estimates are provided for large, medium and small firms. Accordingly, each population estimate has been separated out into three sub-populations.

We discuss how the total population was altered in the context of each technical standard when providing the cost estimates. As an example, for the technical standards relating to objective presentation and disclosure of conflicts of interest, we adjusted the relevant population to include only large and medium-sized sell-side institutions who we anticipated would be affected by the draft technical standards, as they

[39] Available on Eurostat.

are likely to be the sell-side firms responsible for the vast majority of investment research produced — with the population estimate reduced accordingly.

6 Appendix — Questionnaire Content

Basis for comparison

The additional costs and impacts of ESMA's technical standards should be considered against your firm's current compliance practices.

Any changes to your organisation made as a result of the MAR or in anticipation of ESMA's technical standards should not form part of your consideration of you firm's current compliance practices. For example, if you were not covered under the Market Abuse Directive (MAD), are newly-covered under the MAR, and have made any operational changes or investments in anticipation of new regulatory requirements affecting your business, do not consider these as part of your responses. Instead, focus on the costs and affects arising from ESMA's technical standards for implementing the MAR only.

Section 1: Firm profile and background

1. In the last financial year, what was the total revenue for your firm?
2. In the last financial year, what was the total operating expenditure for your firm?
3. How many employees in the European Union does your firm have?
4. Of those employees working in the European Union, how many work in the compliance function?
5. How would you categorise your firm's core business line? Please select the most appropriate option below.
    a. Sell-side (debt capital markets, equity capital markets, sales and trading, investment research)
    b. Independent broker / dealer
    c. Buy-side (investment management)
    d. Non-financial corporate that issues debt and / or equity
    e. Trading venue
    f. Other (please elaborate)

Section 2: ESMA's draft technical standards – compliance costs and wider impacts

Share buy-backs and stabilisations

6. What processes would you need to undertake to comply with ESMA's standards for share buy-backs and stabilisations? For example:

	Yes	No	Maybe
a. Train staff on new regulatory requirements			

b. Develop additional IT systems infrastructure or upgrade existing infrastructure

c. Revise the organisational structure of the firm

d. Redesign or increase your capacity for reporting to Competent / Regulatory Authorities

e. Employ external professional services (e.g. consultancy, legal services, etc.)

f. Other

7. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements		
Develop additional IT systems infrastructure or upgrade existing infrastructure		
Revise the organisational structure of the firm		
Redesign or increase your capacity for reporting to Competent / Regulatory Authorities		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

8. Do you believe that the requirement to report to multiple Competent Authorities, rather than a single Competent Authority, will affect the number of venues on which you or your clients would list or trade securities? If so, why?

9. Do you believe that the requirement to report to multiple Competent Authorities, rather than a single Competent Authority, will affect the number of venues on which you or your clients would conduct buy-backs or stabilisations? If so, why?

10. Do you believe that the fact that buy-backs will not enjoy safe harbour status on OTC markets would affect you or your clients' willingness to trade on OTC venues or OTC activity generally? If so, why?

11. Do you believe that the fact that only purchases, and not sales, of securities will benefit from safe harbour status in stabilisations will impact how you or your service provider will conduct stabilisations?

Market soundings

12. What processes would you need to undertake to comply with ESMA's standards for market soundings? For example:

	Yes	No	Maybe
a. Train staff on new regulatory requirements			
b. Develop additional IT systems infrastructure or upgrade existing infrastructure			
c. Revise the organisational structure of the firm			
d. Development, review, and maintenance of sounding scripts			
e. Due diligence in assessing information in market soundings			
f. Employ external professional services (e.g. consultancy, legal services, etc.)			
g. Other			

13. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements		
Develop additional IT systems infrastructure or upgrade existing infrastructure (e.g. for recording keeping purposes, particularly with respect to due diligence and processes on market soundings)		
Revise the organisational structure of the firm		
Development, review, and maintenance of sounding scripts		
Due diligence in assessing information in market soundings		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

14. Do you believe that the requirements on DMPs proposed in the technical standards will impact your or your potential counterparties' willingness to conduct market soundings as DMP / the confidence in the market sounding process?

15. Do you believe that the lack of a cleansing strategy will impact your or your potential counterparties' willingness to be sounded? If so, why?

16. If fewer potential investors are sounded, do you believe this will affect the quality of information used in the pre-transaction process? If so, how would this affect your transaction activity?

Suspicious transaction and order reporting (STOR)

17. What processes would you need to undertake to comply with ESMA's standards for suspicious transaction and order reporting? For example:

	Yes	No	Maybe
a. Understanding the standard and its requirements			
b. Train staff on new regulatory requirements and to ensure that the appropriate culture of staff is maintained			
c. Develop additional IT systems infrastructure or upgrade existing infrastructure			
d. Revise the organisational structure of the firm			
e. Additional investigation of suspicious activities / "near misses"			
f. Maintain records for an extended period of time			
g. Reporting to Competent / Regulatory Authorities			
h. Employ external professional services (e.g. consultancy, legal services, etc.)			
i. Other			

18. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements and to ensure that the appropriate culture of staff is maintained		
Develop additional IT systems infrastructure or upgrade existing infrastructure		
Revise the organisational structure of the firm		
Additional investigation of suspicious activities / "near misses"		
Maintain records for an extended period of time		
Reporting to Competent / Regulatory Authorities		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

19. Do you believe that the STOR policy will affect smaller firms to a greater extent than larger firms? If so, why?

20. Do you believe that the STOR may affect order sizes, for example resulting in large orders being placed across multiple counterparties? If so, why?

Technical means for public disclosure of inside information and delays

21. What processes would you need to undertake to comply with ESMA's standards for public disclosure of inside information and delays? For example:

	Yes	No	Maybe
a. Understanding the standard and its requirements			
b. Train staff on new regulatory requirements			
c. Develop additional IT systems infrastructure or upgrade existing infrastructure			
d. Revise the organisational structure of the firm			
e. Conduct additional internal reporting			
f. Redesign or increase your capacity for reporting to Competent / Regulatory Authorities			
g. Employ external professional services (e.g. consultancy, legal services, etc.)			
h. Other			

22. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements		
Develop additional IT systems infrastructure or upgrade existing infrastructure		
Revise the organisational structure of the firm		
Conduct additional internal reporting		
Redesign or increase your capacity for reporting to Competent / Regulatory Authorities		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

23. Do you believe the fact that EAMPs face similar but differing requirements under the MAR and REMIT will lead to undue costs or duplication of efforts? If so, why?

24. Do you believe that aligning the dissemination requirements for non-Regulated Market issuers (i.e. MTFs and OTFs) with those of Regulated Market issuers under the Transparency Directive will

affect the costs or attractiveness of listing on such markets relative to Regulated Markets? If so, do you believe this will affect your or your clients' willingness to list on non-Regulated Markets?

Format of insider lists

25. What processes would you need to undertake to comply with ESMA's standards for the format of insider lists? For example:

	Yes	No	Maybe
a. Understanding the standard and its requirements			
b. Train staff on new regulatory requirement			
c. Develop additional IT systems infrastructure or upgrade existing infrastructure			
d. Revise the organisational structure of the firm			
e. Development, review, and maintenance of insider lists			
f. Redesign or increase your capacity for reporting to Competent / Regulatory Authorities			
g. Employ external professional services (e.g. consultancy, legal services, etc.)			
h. Other			

26. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements		
Develop additional IT systems infrastructure or upgrade existing infrastructure		
Revise the organisational structure of the firm		
Development, review, and maintenance of insider lists		
Redesign or increase your capacity for reporting to Competent / Regulatory Authorities		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

27. Do you anticipate any wider effects on your operations or the evolution of the market arising from ESMA's technical standards?

Format of transactions of those with managerial responsibility with an issuer

28. What processes would you need to undertake to comply with ESMA's standards for the format of transactions of those with managerial responsibility with an issuer? For example:

	Yes	No	Maybe
a. Understanding the standard and its requirements			
b. Train staff on new regulatory requirement			
c. Develop additional IT systems infrastructure or upgrade existing infrastructure			
d. Revise the organisational structure of the firm			
e. Development, review, and maintenance of PDMR lists			
f. Redesign or increase your capacity for reporting to Competent / Regulatory Authorities			
g. Employ external professional services (e.g. consultancy, legal services, etc.)			
h. Other			

29. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements		
Develop additional IT systems infrastructure or upgrade existing infrastructure		
Revise the organisational structure of the firm		
Development, review, and maintenance of PDMR lists		
Redesign or increase your capacity for reporting to Competent / Regulatory Authorities		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

30. Do you anticipate any wider effects on your operations or the evolution of the market arising from ESMA's technical standards?

Objective presentation and disclosure of interest or conflicts of interest by those producing or disseminating investment recommendations or investment strategies

31. What processes would you need to undertake to comply with ESMA's standards on objective presentation and disclosure of interest or conflicts of interest by those producing or disseminating investment recommendations or investment strategies? For example:

	Yes	No	Maybe
a. Understanding the standard and its requirements			
b. Train staff on new regulatory requirement			
c. Develop additional IT systems infrastructure or upgrade existing infrastructure			
d. Revise the organisational structure of the firm			
e. Compile additional detail on the investment recommendation process (e.g. valuation models)			
f. Compile detail on additional disclosures (e.g. past recommendations, long and short positions)			
g. Redesign or increase your capacity for reporting to Competent / Regulatory Authorities			
h. Employ external professional services (e.g. consultancy, legal services, etc.)			
i. Other			

32. What one-off and ongoing costs would be associated with these processes?

	One-off Costs (Local Currency Unit)	Ongoing Costs (Local Currency Unit)
Understanding the standard and its requirements		
Train staff on new regulatory requirements		
Develop additional IT systems infrastructure or upgrade existing infrastructure		
Revise the organisational structure of the firm		
Compile additional detail on the investment recommendation process (e.g. valuation models)		
Compile additional detail on additional disclosures (e.g. past recommendations, long and short positions)		
Redesign or increase your capacity for reporting to Competent / Regulatory Authorities		
Employ external professional services (e.g. consultancy, legal services, etc.)		
Other		

33. Do you believe that the proposed requirements will lead to delays in releasing investment recommendations or opinions? If so, which requirements have most impact and how would this affect the attractiveness of European capital markets versus foreign capital markets?

34. Do you believe that the requirement to disclose information on valuation models will affect firms' willingness to develop new valuation approaches and/or will lead to an increase in client queries

regarding valuation models used? Do you believe that the requirement will impact the number of differing opinions in the market?

35. Do you believe that the lack of a quantitative threshold for what constitutes a 'large number of persons' and hence is classed as public disclosure will impact the research and investment recommendation process? If so, how?

36. Considering now <u>all</u> of the Technical Standards discussed above, what benefits from the requirements proposed by ESMA are there for you and your clients?

7 Appendix — Background Information provided to Survey Participants

At a high level, ESMA's draft technical standards relate to:

- buy-back programmes and stabilisations;
- market soundings;
- detection, prevention, and reporting of suspicious orders and transactions;
- disclosure of inside information and delays to such disclosure;
- insider lists;
- transactions by persons discharging managerial responsibilities; and
- the objective presentation and the disclosure of interests/conflict of interests in investment recommendations.

We discuss each category below. Our primary basis for this discussion is ESMA's July 2014 Consultation Paper on the draft technical standards.[40] Please refer to that document for more detail.

7.1 Buy-back programmes and stabilisations

Issuers purchasing their own shares can be market abusive, e.g. an investor or institution purchasing a security with the aim of supporting the security's price. However, there are legitimate reasons for stabilising a financial instrument or an issuer to trade in its own shares, justifying that such trades would be exempt from the insider trading and market manipulation prohibitions set out in other areas of the MAR[41] providing that certain conditions are met (the "safe harbour principle"). ESMA has specified in the technical standards specific conditions that must be satisfied in order to benefit from the safe harbour principle, which we discuss below.

7.1.1 Technical standards

Buy-back programmes

For a buy-back programme to benefit from the safe harbour principle, MAR requires that it must "have as its sole purpose:

- to reduce the capital of an issue; or
- to meet the obligations arising from debt financial instruments that are exchangeable into equity instruments; or

[40] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation".
[41] This was also the case in Article 8 of the Market Abuse Directive (MAD).

- to meet obligations arising from share option programmes, or other allocations of shares, to employees or to members of the administrative, management, or supervisory bodies of the issuer or associate company."[42]

Where a buy-back programme does have one of the above as its sole purpose, the buy-back programme can benefit from the safe harbour principle where:

- The full details of the programme are publicly disclosed prior to the start of trading — ESMA has defined the relevant details to be disclosed in Article 3(1) of the draft technical standards.[43]
- The buyback transactions are reported to the Competent Authority and publicly disclosed.[44]

For general public disclosure, ESMA requires that data are published via the website of the issuer conducting the buy-back programme and disseminated through appropriate disclosure channels. For shares trading on Regulated Markets, current practices — that is, those established through the Transparency Directive — for dissemination and storage are sufficient. In other words, there should be no change with respect to current market practices. For other issuers not covered under the Transparency Directive, i.e. multilateral trading facilities (MTFs) or organised trading facilities (OTFs) only issuers, they will need to disclose the information via the mechanisms and channels set out in that Directive. Aggregated daily repurchase volumes and volume-weighted average purchase price per venue will be displayed on the issuer's website no later than the end of the seventh market session[45] following the date of the execution of the reported transactions.

For disclosure to Competent Authorities, detailed transaction information will be provided for every transaction, rather than the aggregated information provided to the general public, and no later than the end of the seventh market session. The "investment firms concerned" will refer to the investment firm that is conducting the buy-back on behalf of the issuer, rather than the counterparty selling the securities. Issuers will need to report information on buy-back activity to the relevant Competent Authority for each registered market or multilateral trading facility on which the buy-back is conducted.

The price limit and volume conditions defined in the ESMA technical standards (TS) are complied with

Shares cannot be repurchased at a price higher than the highest previous independent trade or the highest existing bid price.[46] These price limitations apply for the venue on which the buy-back will occur. Share buy-backs will enjoy safe harbour status only on registered trading venues and not in over-the-country (OTC) markets.

If an issuer's shares are traded continuously throughout the day, then buy-backs during a share auction would not fall under the safe harbour principle. If, however, the shares trade on an auction-only market (i.e. not continuously), then buy-backs executed during an auction benefit from safe harbour, but such orders cannot be placed during the last instant before the end of an auction.

Buy-backs cannot exceed 25 per cent of the daily average volume of shares traded over a period of reference and there is no longer allowance for exceeding this 25 per cent threshold in situation of "extreme low liquidity" as under the current MAD regime. Daily averages will be calculated for the venues in which the share buy-backs will be conducted.

[42] Article 5(2) of: Council Regulation (EC) 596/2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC [2014] L173/1 (referred to throughout as "the MAR").

[43] These are the fields to be reported under the current regime.

[44] Information on the content of these disclosures is specified in Article 5(3) of MAR.

[45] The rule on timing for reporting buy-backs is the same as the requirement under the MAD.

[46] This is the same as under the current regime.

The transactions executed that do not fall under a restriction defined in the TS

An issuer that is conducting a share buy-back cannot sell shares during the buy-back programme unless the programme is time scheduled, lead managed independently by an investment firm / credit institution, or, in the case of buy-backs by investment firms / credit institutions, an appropriate "Chinese Wall" is in place between those selling shares and those executing the buy-back programme. For these restrictions and exemptions for own-trading in shares, ESMA reuses the restrictions (and the exemptions to them) currently in place under MAD.

Stabilisation measures

Stabilisations involve the purchase of a security with the aim of supporting the security's price. According to MAR,

> "stabilisation" means a purchase or offer to purchase securities, or a transaction in associated instruments equivalent thereto, which is undertaken by a credit institution or an investment firm in the context of a significant distribution of such relevant securities exclusively for supporting the market price of those securities for a predetermined period of time, due to a selling pressure in such securities. The term "significant distribution" is further defined in Article 3(2)(c) of MAR as an initial or secondary offer of securities that is distinct from ordinary trading both in terms of the amount in value of the securities to be offered and the selling method to be employed.[47]

Unlike buy-backs, instruments other than shares, such as convertible and non-convertible fixed income securities, can be purchased under stabilisations.

In order to benefit from the safe harbour principle, stabilisation measures and transactions must be comply with certain conditions specified in the ESMA technical standards, that are essentially similar to those in place under the current regime.

There are different timing restrictions for different classes of securities. For newly-issued shares and securities equivalent to shares, stabilisations may not last longer than 30 days after the shares began trading on the relevant market or the final opening price has been disclosed (for Member States that permit trading in shares before formal issuance). For secondary offerings, stabilisations should begin on the date of disclosure of the final price and may not last longer than 30 days following the allotment date.

For non-convertible and convertible fixed income instruments, stabilisations should begin when the terms of the security are publicly disclosed and end either 30 calendar days after the issuer receives the proceeds of the issuance or 60 calendar days after the allotment of the securities, whichever is shorter.

For securities covered by the Prospectus Directive, ESMA considers the requirements imposed by that Directive sufficient to ensure adequate disclosure of stabilisation activity to market participants. For securities not covered by that Directive, ESMA will require the beginning and end of the stabilisation period be disclosed to market participants as well as the fact that stabilisation purchases may support the market price during this period. Furthermore, the identity of the entity undertaking that stabilisation on behalf of the issuer — known as the "stabilisation manager" — must also be disclosed, as well as any overallotment facility. This disclosure is under the responsibility of <u>one person</u> appointed by the issuer, offeror and the stabilisation manager among themselves.

Within a week after the stabilisation period has ended, the stabilisation manager must disclose whether stabilisation purchases have taken place, the start and ending date for the period over which the purchases had taken place, and the price range for the purchases.

[47] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 12.

As with buy-backs, stabilisation disclosures must be reported to each relevant Competent Authority for the markets on which the stabilisation purchases are made and must be disclosed no later than seven market sessions after the date of the transaction in question.

The above reporting obligations must be fulfilled by the stabilisation manager, rather than the issuer. If a consortium is managing the stabilisation activities, then one consortium member should act as a central contact point for transparency-related functions.

Shares cannot be purchased above the prevailing market offer price and fixed income securities cannot be purchased above the market price of those securities at the time of public disclosure of the terms for the new issuance.

Where an overallotment facility exists under a "Greenshoe option" in the underwriting agreement, securities purchased under this facility cannot represent more than 15 per cent of the original offer volume. If there is overallotment not covered by the "Greenshoe option", the overallotment cannot represent more than 5 per cent of the original offer volume.

Transactions benefitting from safe harbour status as stabilisation transactions can only be purchases, rather than sales, since purchases are the only transactions that would support the share price. Additionally, block trades do not enjoy safe harbour status.

7.2 Market soundings

The MAR defines a market sounding as "a communication of information, prior to the announcement of a transaction, in order to gauge the interest of potential investors in a possible transaction and the conditions relating to it such as its potential size or pricing, to one or more potential investors."[48] The entity that makes a market sounding is a "disclosing market participant" (DMP).

Market soundings can contain inside information and, for that reason, can constitute or lead to market abuse. To protect themselves from such charges during the course of legitimate business activities, DMPs are required to comply with ESMA's technical standards on market soundings.

7.2.1 Technical standards

ESMA's technical standards can be broken down into two broad categories. These are standards relating to activities prior to conducting market soundings and requirements and procedures when conducting market soundings.

We describe each in turn below.

Activities prior to market soundings

Article 11(3) of the MAR obliges DMPs to assess whether or not information to be contained in a market sounding is indeed inside information and to keep written documentation on the reasons underlying the conclusion of this assessment.

These obligations fall on the DMP and are further specified in the technical standards. The assessment will also involve determining when the transaction related to the market sounding is estimated to be made public although there will be no agreed "cleansing strategy" with the potential investor with respect to inside information in market soundings. The DMP is required to keep a record of the pre-market sounding due diligence and disclosure proposals. If the related transaction is being arranged by a syndicate, the DMP should ensure that all syndicate members agree about the characterisation of information as non-inside

[48] Article 11(1) of the MAR.

information. If syndicate members cannot agree on the characterisation, the information will be treated as inside information for the purposes of market soundings.

ESMA has not given explicit recommendations on the number and type of investors to question, other than offer some best practice guidance.[49] Additionally, ESMA notes that the time between the market sounding and the anticipated transaction date should be minimised, but does not provide precise requirements for how long the time should be or how it should be minimised.

Requirements and procedures when conducting market soundings

DMPs will be required to obtain potential investors' permission to receive inside information related to a transaction prior to making a market sounding. This relates to any one specific transaction, but DMPs are also required to maintain a list of potential investors who have said that they prefer not to be sounded in relation to potential transactions in general. DMPs do not need to continuously contact investors to query their preferences, but should update the list upon information provided by the potential investors should their preference for receiving market soundings has changed.

Records kept during the market sounding process are required to be kept in a durable medium. DMPs will need to keep records on all market soundings, not simply those containing inside information.

DMPs are required to develop and maintain a standardised template for conducting market soundings (i.e. scripts). This applies to all market soundings, whether or not they contain inside information. All market sounding scripts are required to contain:

- A statement noting that the communication is a market sounding.
- A confirmation that the DMP is communicating with the appropriate individual.

In the case of a market sounding that contains inside information, scripts will contain:

- A statement that the DMP has assessed the information contained within the sounding and has deemed it to be inside information.
- A reminder the potential investor that acceptance of the market soundings obliges the potential investor to keep the information confidential.
- The expected time when the information will cease to be inside information, with a note that this time is subject to change and how the potential investor will be informed when this time changes.
- A reminder to the potential investor that administrative and criminal penalties may apply if the potential investor violates laws regarding inside information.
- A request for consent from the recipient of the market sounding to receive inside information.

In the case of a market sounding that does not contain inside information, scripts will contain:

- A warning to potential investors that, although the DMP has judged the information contained in the market sounding not to be inside information, this could be an incorrect assessment and could become inside information when combined with other information held by the potential investor.
- A statement clarifying that the potential investor must assess the information to determine whether or not information in the market sounding is indeed inside information and, if the potential investor concludes that the information is inside information, the potential investor is bound by legal restrictions regarding inside information.
- A request for consent from the recipient to be sounded.

DMPs are required to keep lists of individuals that have received the market sounding. This list contains individual information only on the individual that received the market sounding, rather than employees to whom the market sounding information was subsequently distributed. The list will contain:

[49] For instance, a syndicate should ensure that a single investor is not questioned by several different syndicate members about the same transaction.

- Names of the firms and individuals at the firm who were sounded.
- The date and time of the initial sounding and any follow-ups.
- Contact details employed in the sounding.

The DMP will maintain contact details for a point of contact at potential investors for market soundings and will contact only that individual for market soundings (unless such information is out of date).

All market sounding communication between DMPs and potential investors must be recorded. For fixed line and mobile telephony, this must take the form of recording conversations. For meetings, a sufficient written account of the items discussed and the conclusions of the meeting must be kept as well as information on dates, times, meeting attendees, whether or not the DMP market sounding script was executed. The content of the meeting record should be confirmed by all parties involved, such as obtaining signatures of potential investors. Alternatively, meetings can also be video recorded, in which case a signature would not be necessary.

DMPs are required to develop and maintain operational procedures for conducting market soundings. These procedures must be reviewed periodically and updated as needed. DMPS are required to take the necessary steps to:

- limit the employees involved in conducting market soundings;
- ensure that these employees have proper training;
- limit the number of employees that have access to information contained in the market sounding; and
- reduce the time between disclosing information to employees conducting market soundings and sounding potential investors.

7.3 Suspicious transaction and order reporting (STOR)

While not all suspicious transactions will reflect cases of market abuse, by definition they may be indicative of market abuse. It is therefore a requirement of MAR that trading venues "establish and maintain effective arrangements, systems and procedures for preventing and detecting market abuse and attempted market abuse". Those arranging and executing transactions ("firms") also have a similar requirement regarding suspicious transactions and orders. MAD and ESMA guidance has previously addressed suspicious transactions reporting, with ESMA drawing on this work as part of its proposals.

7.3.1 Technical standards

The reporting obligations

Article 16 of the MAR states that "firms" and operators of trading venues are required to report all orders and transactions which may constitute market abuse. This includes suspicious activities where orders have been cancelled, modified or not executed. Effective arrangements must be in place to detect and report any suspicious orders and transactions. Reporting is also required regardless of whether a transaction takes place on a trading venue or OTC.

Timing and level of suspicion required

Articles 16(1) and (2) require reporting of suspicious transactions to occur "without delay". In the discussion paper ESMA indicates that "without delay" would generally mean that the Competent Authority is notified within two weeks of suspicion being aroused. ESMA states that STORs may be reported by telephone and then followed up with written confirmation in the appropriate form in order to facilitate the timely reporting of STORs.

There will be no "batching" of reports, where a market participant waits until a sufficient number of suspicious transactions or orders have been submitted before notifying a Competent Authority.

ESMA suggest that entities should only base their suspicion on what they observe, rather than what they may infer, such as if they are aware that a client using multiple brokers. Where a chain of market participants are involved in a transaction, they all have an obligation to make STORs, rather than one entity in the chain absolving the responsibility from other entities.

Detection

Article 16 requires firms to have systems and procedures in place which aim to detect suspicious market activity. Although for smaller entities ESMA does not require this system to be automated, above a certain size, firms may be required to implement automated systems in order to comply with the regulation. Besides, firms will need to have appropriate training of their staff to develop a proper detection and reporting culture but ESMA is not prescribing details of this as it needs to be tailored to the size of the firm.

Content of STORs and STOR template

As required under Article 16(5), ESMA is proposing a notification template for STOR. The proposed single harmonised reporting form, in electronic format, allows to fulfil completely with the requirements of Articles 16(1) and 16(2) and is structured in such a way that the relevant Competent Authority is able to easily follow up on any reports or share it with other authorities.

Record-keeping

ESMA proposes that a record of STORs should be kept for five years. "Near-misses", where potentially suspicious transactions which have been examined but not deemed sufficiently suspicious and so are not reported to a relevant Competent Authority, should also be maintained since these should provide some indication as to whether firms are in compliance with the technical standards.

7.4 Technical means for public disclosure of inside information and delays

The public disclosure of inside information helps to ensure the efficiency of financial markets, since it enables market participants to disseminate relevant information which should be reflected in the value of financial instruments.

The timely disclosure of inside information also helps to mitigate the likelihood of insider trading, since it reduces the timespan over which insider trading may occur.

Article 17 of MAR expands upon article 6 of MAD. Issuers of financial instruments are required under MAR to disclose inside information publicly as soon as possible. Information is also required to be distributed in such a way that it "enables fast access and complete, correct and timely assessment of the information". The disclosure of public information is currently required under MAD by issuers of financial instruments admitted to trading on a Regulated Market (RM). Under MAR this is to be expanded to include:

- issuers of financial instruments only traded on a MTF where these issuers have requested admission to trading on a MTF or have approved trading on an MTF or an OTF;
- issuers of financial instruments only traded on an OTF where these issuers have requested admission to trading on an MTF or have approved trading on an MTF or an OTF; and
- emission allowance market participants, unless they do not meet a threshold to be set by the European Commission.

7.4.1 Technical standards

ESMA has developed a number of technical standards for the means for public disclosure of inside information and means for delaying the disclosure inside information. We describe both in turn below.

Technical means for public disclosure of inside information

Article 17(1) obliges issuers of financial instruments to publicly disclose inside information as soon as possible in a way that facilitates easy access and complete, correct, and timely assessment of the information by the public. Requirements in Article 17(1) are the same as those under the MAD, so issuers currently operating under the MAD will face similar requirements under the MAR. Issuers covered by the Transparency Directive — i.e. those issuers trading on Regulated Markets — will also need to disclose the inside information in the official appointed mechanism (OAM).[50] Emission allowance market participants (EAMPs) are also required to publicly, effectively and in a timely manner disclose inside information.

Besides, MAR requires all issuers, whether subject to the Transparency Directive or not, must post disclosed inside information on their websites and maintain it there for a minimum of five years. For issuers on small and medium sized enterprise (SME) growth markets, MAR allows these issuers to post the information on the SME growth market trading venue's website rather than their own websites. ESMA contends "it is assumed that inside information should remain published on the SME Growth market operator's website for at least five years". However, EAMPs are not required to post all inside information on the issuer's website for five years.[51]

ESMA proposes that requirements, standards, mechanisms, and channels relating to dissemination of information set out in the Transparency Directive are used by all issuers under MAR for the public disclosure of inside information. For issuers on Regulated Markets, this implies continuity with current practices. However, for others covered under the MAR, this represents a new requirement. The public disclosure should occur without delay. This also holds for EAMPs without preventing them from using a Regulation on wholesale Energy Market Integrity and Transparency (REMIT) disclosure channel provided it satisfies these requirements.

Disclosure via other means, such as social media or publication in a newspaper, would not meet the requirements for proper dissemination. Posting inside information on the relevant Competent Authority's website only would not be sufficient to comply with the MAR "unless the Competent Authority's means for disclosure of inside information meet the requirements of proper dissemination and of appropriate public disclosure set out in the [Transparency Directive]."[52]

ESMA notes that "the website where inside information is posted by the issuer in fulfilment of Article 17(1) and 17(9) [of the MAR] should have the following technical features:

- The access to the website should be non-discriminatory and free of charge.
- Inside information should be easy to find…
- Considering the five year record keeping, previously disclosed inside information should be easy to find, for instance via an archive-type tool; disclosed information should notably be clearly dated."[53]

Technical means for delaying the disclosure of inside information

The MAR lays out two types of delays to the disclosure of inside information: "general" delays and delays to preserve the stability of the financial system.

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50 Issuers on other types of trading venues not covered by the Transparency Directive, such as MTFs or OTFs, do not have to use the OAM, which a storage mechanism under the Transparency Directive.
51 ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 57.
52 ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 54.
53 ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 58.

With respect to "general" delays, the MAR requires that Competent Authorities be informed by issuers or EAMPS *ex-post* about the existence of a delay and a written explanation on how conditions to be met when delaying the disclosure of inside information were met. The MAR does allow for the possibility of this latter explanation to be provided only upon request of the Competent Authority, if allowed by national law. The existence and explanation disclosures should take place immediately.

ESMA considers that the act of notifying the Competent Authority should be integrated into the issuer's general process for disclosing inside information. These notifications should be provided in writing via a secure electronic transmission mechanism to a dedicated contact point at the Competent Authority. The Competent Authority should make the notification process clear to issuers.

With respect to information provided about the delay, ESMA proposes to include the following information in the notification sent to the Competent Authority:

- "the identity of the issuer: full official name;
- the identity of the person within the issuer making the notification (name, surname, position, contact details: emails, professional phone number);
- identification of the disclosed insider information that was delayed (title of the disclosure statement, reference number assigned by the dissemination system if available);
- date and time of the public disclosure of the relevant inside information;
- date and time of the decision to delay the disclosure of inside information;
- the identity of the persons having taken part in the decision making process for delaying."[54]

The time stamp on the communication should specify the time zone and be as granular as possible.

If the explanation is sent after, rather than with, the delay notification, the above information should be provided with the explanation as well.

To demonstrate that the conditions for legitimate delays to disclosing inside information set out in Article 17(5) of the MAR are met, ESMA proposes that issuers submit the explanatory notification around three conditions, completed in free text:

- "describing the legitimate interest at stake;
- specifying [the issuer's] assessment on how the omission of the inside information would not be likely to mislead the public;
- describing how the confidentiality of the delayed inside information is ensured, notably what information barriers have been put in place internally for non-required persons within the issuer vis-à-vis third parties. Without prejudice of the need to identify the persons within the issuer who decided about the delay, it is not considered necessary to name the persons within the issuer who has access to this delayed information, as they should already be included in the insider list."[55]

When there is a change with respect to how the conditions were originally met, a new assessment of the conditions and the assessment's timing should be included in the explanation.

The notification should be drafted in the language in which the inside information is disclosed. The exception to this is notifications for EAMPs, which could either be made in a language accepted by the Competent Authority and a "language customary in the sphere of international finance" or only in the latter

In terms of record keeping, issuers are expected to have an organisational structure and processes in place to conduct an assessment of whether information is inside information, whether or not to delay disclosure, and, if the issuer decides to delay, how long the delay should be. There should be a responsible person or set of persons with sufficient capacity and seniority to make such a decision within the organisation. It is

[54] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 59-60.
[55] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 60.

this person or these persons who conduct an assessment of whether the three criteria under Article 17(4) of the MAR with respect to inside information are satisfied. Furthermore, there should be an assessment of when the delay should end, how the inside information is disclosed, and how disclosure and notification to the Competent Authority has been achieved. The issuer must monitor on an ongoing basis whether the conditions justifying the delay remain. In the event that there appears to be a breach of confidentiality, the information must be immediately disclosed to the public.

All of these processes require records to be kept by the issuers. ESMA's draft technical standards propose that the following internal records be kept:

- "the process for assessing and deciding on the starting and ending point of delaying the inside information;
- the fulfilment of the conditions for delay, both initially and on an on-going basis during the delay period, are set up and kept under regular view (a new record is needed just when there has been a change in the original conditions);
- responsibilities within the issuer are clearly allocated…
- the delayed inside information is properly handled and managed within the issuer as well as with respect to third parties in order to limit to the extent possible, if not avoid, any breach of confidentiality during the delay period."[56]

Additionally, ESMA specifies that the issuer should keep records of the means put in place to:

- "deny access to non-required persons;
- ensure awareness of the persons accessing delayed inside information about the legal and regulatory duties as well as of the sanctions attached ; and
- immediately disclose the inside information in case of breach of confidentiality".[57]

ESMA believes that the more individuals that are involved in handling the inside information, the more stringent the processes in place should be.

Delays to preserve the stability of the financial system

For some issuers, such as credit institutions and financial institutions, the MAR allows for delays to preserve the stability of the financial system. These delays require notification *ex-ante* and must be agreed by the Competent Authority in advance. The technical means for recording this type of delay are the same as those for "general" delays. However, given the highly sensitive nature of the information, ESMA suggests the secure communication channels are used between issuers and Competent Authorities.

The issuer's notification to the Competent Authority of intent to delay disclosure of inside information should be made in writing. The Competent Authority should inform the issuer of their decision to grant or not to grant consent for the disclosure. This can be done orally initially, but should be followed up followed up with the decision in writing without delay.

The issuer and the Competent Authority should inform one another of any new development, event, or information that could affect the fulfilment of conditions for delaying disclosure.

7.5 Format of insider lists

The creation, maintenance and update of insider lists is a means of detecting and preventing individuals with access to market sensitive information from utilising this information to their benefit, such as for unfair gain. Article 18 of the MAR specifies the creation of such lists comprising all individuals directly employed by issuers, or else engaged in an indirect role, such as accountancy or advisory services. The insider list

[56] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 62.
[57] ESMA (2014) "Consultation paper: draft technical standards on the Market Abuse Regulation", p. 62.

requirements also apply to EAMPs, auction platforms, auctioneers, and the auction monitor. ESMA, in turn, has drafted technical standards regarding the specific format of these insider lists and the means by which they must be updated.

7.5.1 Technical standards – insider lists

Content

Article 18 specifies that the insider list should include the identity of any individual with access to inside information. In this regard, ESMA has specified that the following personal information should be disclosed in insider lists:

- Name: first name, surname and birth surname.
- Full home and work address.
- National Identification, or the date and place of birth (this will depend on the Member State).
- Home, work and mobile telephone numbers.
- Personal and work e-mail addresses.

The function of each insider must also be specified, as well as the company name for those insiders employed by third parties working for the issuer. The insider lists must also specify the exact date and time (including time zone) at which the individual gained access to the inside information in question, and the exact date and time at which access to this information ended.

Coverage

In terms of the types of person with access to inside information that must be included in insider lists, ESMA proposes the following:

- Member of the management and/or supervisory board.
- Executive officers.
- Individuals discharging management responsibilities.
- Related staff members (e.g. personal assistants).
- Internal auditors.
- Individuals who can access information on budgets and balance sheets.
- Individuals operating in areas with regular access to inside information.

Third party professionals subject to the regulation include: auditors, attorneys, accountants, managers of issuers, ratings agencies, investment analysts and tax advisors. ESMA's list in this regard is to be considered indicative and non-exhaustive.

Format of the insider lists and delivery

ESMA adopts a flexible approach to how the insider lists can be set up within the issuer, EAMP, auction platform, auctioneer, and auction monitor and presented to the relevant Competent Authority:

- A general list encompassing all insiders involved in the relevant projects of an issuer.
- A deal-specific list detailing the insiders in relation to a specific set of inside information.

There is also flexibility as to whether the issuer includes the insider lists of related third parties with their own insider list, or simply submits them as separate insider lists.

ESMA requires the insider lists to be submitted in the language of the relevant Competent Authority or a language customary in international finance. Furthermore, the lists must be in a secure electronic format which can be computer read and processed, although the exact format that must be used is not specified.

Maintaining and updating

The insider lists should be kept by the insider for a minimum period of five years since the last point of update. This means that when updates to the list take place, the previous insider list should not be overwritten, but rather a new version of the list should be created, such that the issuer keeps on record the content of the insider lists at different points in time. When circumstances change, the insider lists should be updated accordingly and without unnecessary delay. However, ESMA's proposals do not specify the nature of governance procedures that must be in place to ensure this. Relevant insider lists should be provided without delay on request by the Competent Authority.

Exemption for SME growth market issuers

Issuers on SME growth markets are exempt from creating, maintaining and updating a contemporaneous insider list under Article 18 of the MAR under the condition that they can provide an insider list upon request of the Competent Authority. In this respect, ESMA proposes that they are required to submit an insider list containing the appropriate information and in the proper format.

7.6 Format of transactions with managerial responsibility with an issuer

Individuals in management roles are likely to possess undisclosed, market-sensitive knowledge about the performance and strategic direction of their employer. Transactions based on such knowledge of inside information would constitute market abuse. Therefore, persons discharging managerial responsibilities (PDMRs) and those closely associated to them (closely associated persons) must notify their employer and the relevant Competent Authority of any transactions in financial instruments linked to their employer. Besides, this information should also be publicly disclosed. In the case of an issuer this encompasses trade in shares or debt instruments of that issuer, or derivatives and other financial instruments linked to these securities. And, in the case of an EAMP, auction platform, auctioneers, or auction monitor this includes transactions relating to emission allowances, as well as auctioned products and derivatives linked to emission allowances.

The obligation to notify and publicly disclose relevant transactions of PDMRs and closely associated persons already existed under MAD, but MAR has extended the scope of this obligation to cover financial instruments admitted to trading, those for which a request has been made to trade on a MTF, and those traded on an OTF. The MAR has also reduced the timeframe for notifying such transactions, from five days to three. As with the insider lists discussed above, ESMA's focus is on defining the specific format of such transaction notifications and publications.

7.6.1 Technical standards – managers' transactions notification and disclosure

Content

ESMA proposes a single template for notification comprising two sections; the first detailing on a transaction-by-transaction basis; and the second providing aggregated figures to be used for publication purpose. ESMA specifies that the following content must be included in the notification:

- Name of person or legal entity, address and contact details.
- The position occupied by the PDMR, and the relationship of the closely associated person for disclosure to the relevant Competent Authority only (not for public disclosure).

- National identification number.
- Details, as set out by MiFIR, on the following; the nature and identification number of the financial instrument; the transaction type; the price and volume; and the date and place of execution.

For aggregation, ESMA proposes that all transactions of a given financial instrument carried out on the same day are aggregated (though not netted), and the weighted average price, as well as the day-high and -low prices, reported

Delivery

With respect the delivery to the Competent Authority and the employer, ESMA proposes that whatever electronic form is used the safety and integrity of the information should not be placed at risk. If a notification needs to be retracted or corrected for errors, then an explanation of this should be provided by the relevant party and the entire notification resubmitted.

ESMA also specifies the channels for ensuring the publication of the aggregated information i.e. the ones to be used by issuers and EAMPs for disclosure of inside information, except when the Competent Authority ensures the publication.

7.7 Objective presentation and disclosure of conflicts of interest

This set of technical standards concerns objectivity in conducting and presenting research, and the disclosure of conflicts of interest when presenting research or investment recommendations. Failure to meet these standards would constitute market abuse. The MAR does not make significant changes to the approach of the MAD. Therefore, in developing draft regulatory technical standards mandated by Article 20(3) of MAR, ESMA is of the view that the current measures in place under MAD are a sound base from which to further develop these standards.

7.7.1 Technical standards

There are five key areas in which ESMA has developed regulatory technical standards:

- regulatory scope;
- date and time of disseminations;
- production of recommendations (including identity of producers, objective presentation and disclosure of interests and conflicts of interest);
- non-written recommendations; and
- dissemination of recommendations by third parties.

The regulatory technical standards developed by ESMA in each area are looked at in turn.

Regulatory scope

ESMA develops a two-tiered approach, in line with the MAR proposals and the existing MAD, as follows:

- General obligations applying to all ‘qualified’ and ‘non-qualified’ persons, as defined by MAR Article 3(1)(34).
- Additional obligations applying to all ‘qualified’ persons, as well as any ‘non-qualified’ persons considered ‘experts’, where an ‘expert’ is defined as someone who repeatedly proposes investment decisions, and either sees himself as possessing financial expertise or experience, or produces recommendations in a way that suggests financial expertise or experience.

Any note that falls under the MAR definition of 'investment recommendations' (Article 3(1)(35)) or 'information recommending or suggesting an investment strategy' (Article 3(1)(34)) is subject to the technical standards. This includes all investment recommendations intended, or expected, to be publicly available, as well as non-personal recommendations delivered to one (or more) clients. However, ESMA does not propose setting a quantitative threshold with regard to what constitutes a 'large number of persons' to further specify public availability.

Date and time of disseminations

Investment recommendations must include the date and time at which the recommendation was first released for distribution.

Production of recommendations

Identity of producers – the technical standards state that all investment recommendations must disclose the name and job title of the person responsible for its production, as well as the name of the person responsible from a legal standpoint. This only applies when the individual is acting in his capacity as an employee. Furthermore, in the case of an investment firm or credit institution or where individual operates under self-regulatory standards, then the disclosure must identify the relevant Competent Authority or self-regulatory standards respectively.

Objective presentation – ESMA applies its two-tiered approach to the standards of objective presentation. These standards are based on those currently in use under MAD.

General standards, applicable to all persons defined under MAR Articles 3(1)(34)(i) and 3(1)(34)(ii), include that; facts and opinions are clearly differentiated; underlying assumptions are presented and projections they generate clearly marked; and reliable sources are used wherever possible and any potential lack of reliability flagged.

ESMA proposes a list of additional standards, applicable to qualified persons defined in Article 3(1)(34)(i) and experts within Article 3(1)(34)(ii), to include that; valuation or methodology involved in setting a price target must be disclosed in summary form; the frequency with which the recommendation will be updated, if at all; and any change in recommendation relative to the last relevant recommendation, including the date of this prior recommendation (providing it is in the previous 12 months). A further obligation for qualified persons and experts is to keep a list of all recommendations made in the preceding year with information on: producer identity, release date, direction of recommendation, market price, target price and period of validity for the recommendation. In terms of disclosing methodologies and assumptions, it is only necessary to do so in the recommendation itself if the methodology or assumptions have changed; otherwise an indication in the recommendation of where such information can be found will suffice. ESMA also encourages methodological consistency for recommendations on related companies/industries. However, when the recommendation is based on a proprietary model, the methodological details of such model must not be disclosed, only the key factors underpinning it and the extent to which its results mark a departure from existing models.

Disclosure of interests and conflicts of interest – ESMA also applies a two-tiered approach to the requirements regarding disclosure of interests and conflicts of interest, adopting the same technical standards as those in the MAD and complementing them. The disclaimers themselves should be clear, accurate and complete and include an indication of the risk of acting on investment recommendations with delay, as the trading position could become outdated.

The general standard (set out in Article 5 of the Implementing Directive 2003/125/EC) mandates the disclosure of any relationship or circumstance — in particular investment in financial instruments which are subject of the recommendation — that may call in to question the objectivity of the investment recommendation. This applies to any person involved, either directly or indirectly, in the production of the recommendation, or else anyone who could feasibly have accessed the recommendation prior to its public dissemination.

The additional obligations (set out in Article 6 of the Implementing Directive 2003/125/EC) for qualified persons and experts are to disclose significant shareholdings and financial interests in any issuer subject of a recommendation, as well as details of the activities engaged in and agreements made with the issuer regarding the recommendation. ESMA proposes that significant shareholdings are defined as holdings in excess of 0.5 per cent of the total issue, compared with 5 per cent under the current regime. This threshold will apply to any long or short positions held in the company. However, in the case that reference is made to specific financial instruments in the recommendation, then no threshold applies and all holdings in these financial instruments must be disclosed.

There are also further disclosure requirements on credit institutions and investment firms including details on the administrative and organisational structure in place to limit conflicts of interest arising, and whether individuals involved in the recommendation purchased or sold shares in the relevant issuer prior to the public offering of those shares. These firms must also disclose, on a quarterly basis, the proportion of buy, hold and sell recommendations and the proportion of issuers applicable to each.

Non-written recommendations

ESMA provides a non-exhaustive list of the modes that non-written recommendations encapsulate, e.g. road shows, radio and TV. The two-tiered objective presentation requirements apply in the same way as for written recommendations and, where relevant, the audience should be made aware of any supporting written recommendations that disclose conflicts of interest in full.

Dissemination of recommendations by third parties

The proposal is that the existing standards under MAD are to apply under the new regime. This states that where significant alterations are made to a third party recommendation, details of such changes should be flagged, and further details given if these changes result in a change in target price or direction of recommendation. The new recommendation should reference the original, as well as providing information with regard to where the disclosures of the original recommendation can be found. Furthermore, intermediaries that disseminate third party recommendations must disclose any relevant interests in accordance with the standards of Article 6 discussed earlier. Disseminating persons are excluded if they belong to the same group as the producer of the recommendation and their role purely concerns transmission and not production.