FCA MAR Review – Periodic Financial Information and Other Issues - Increasing Oversight

In November 2020, the FCA published the findings of its review of MAR compliance and the numbers of delayed disclosure inside information notifications (**DDIINs**) which had been submitted by issuers. The FCA identified a number of areas where lower than anticipated DDIIN submissions could indicate compliance deficiencies with these areas being flagged for increased FCA oversight and awareness raising amongst issuers and their advisers. The FCA has signalled that it will be moving to enforcement action on these points in due course, exposing issuers to the risk of regulatory investigation, fines, censure and reputational damage.

The key areas of focus identified were:

- Periodic Financial Information (**PFI**)
- Unscheduled Financial Information
- Director/Board Changes

The findings revealed a fundamental mismatch between the number of DDIINs received and the FCA's expectations. A summary of the findings and implications is provided below.

In light of the below, our recommendations to Boards are as following:

- review the Company's inside information management and disclosure policy. If you don't have one in writing, consider introducing one.
- re-visit the Company's understanding of "What is Inside Information?" (see below).
- consider refreshing or introducing training on MAR compliance for relevant team members and the Board.
- with PFI, we suggest that early assessment and ongoing review of whether the PFI could include or constitute inside information become part of the routine internal reporting and review process and that this review be documented, even where a decision is reached that the PFI is not inside information. This should be done even where the Company is performing in line with expectations.
- monitor performance against market expectations and conduct an "inside information review" promptly in all cases where the Company is deviating from expectations and an ad hoc trading update may be required.
- assess potential board changes early in the process and plan ahead for the possibility that inside information may arise.

Periodic Financial Information (PFI)

The FCA reminds issuers to start with the assumption that PFI could constitute inside information. PFI includes preliminary results announcements, interim results announcements etc. During the period of review by the FCA (July 2016 to November 2018), only 159 DDIINs were submitted by issuers from over 10,000 PFI announcements. Whilst some misalignment may be due to earlier announcements of specific elements of results which would be considered "inside", this was not borne out by analysis of the numbers of DDIINs submitted in respect of unscheduled financial information.

ONE Advisory's view is that, as market expectations are generally set and priced in ahead of any PFI being released, issuers have considered that results in line with expectations will not "significantly" affect the price and therefore are not inside information. Indeed, the FCA found the average associated share price movement for PFI was around 3%. The FCA comment in their review however that they expected issuers would treat PFI as inside "*regardless of how they compare to market expectations*". The FCA has also noted that a "significant" effect on share price should be interpreted as "non-trivial".

Issuers should also note that MAR, having included price sensitivity as one of the three elements of inside information, then goes on to state that price sensitive information means "*information a reasonable investor would be likely to use as part of the basis of his or her investment decisions*".

It elaborates further that:

"Reasonable investors base their investment decisions on information already available to them, that is to say, on ex-ante available information. Therefore, the question whether, in making an investment decision, a reasonable investor would be likely to take into account a particular piece of information should be appraised on the basis of the ex-ante available information. Such an assessment has to take into consideration the anticipated impact of the information in light of the totality of the related issuer's activity, the reliability of the source of information and any other market variables likely to affect the financial instruments […] in the given circumstances."

In our view the MAR drafting makes the judgement harder for issuers as the two concepts are not necessarily always in alignment and it is not completely clear how they interact - an annual report in line with market expectations may not be particularly price sensitive, but it would be an unusual investor who did not refer to it in making an investment decision. However, given the FCA's stance, it is clear that this reasonable investor test must still in each case inform the issuer's consideration of whether information is "inside" or not.

In terms of process the FCA provided the following advice (TN 506.2 - FCA/TN/506.2 - April 2019):

"When preparing periodic financial reports, issuers should assess on an ongoing and case-by-case basis whether the information they hold fulfils the criteria defining inside information as set out in Article 7 of MAR. In undertaking this assessment, issuers should begin from the assumption that information relating to financial results could constitute inside information.

The FCA expects issuers to exercise judgment and to conduct this ongoing assessment in good faith. Issuers should record and be able to submit evidence of the assessment process to the FCA upon request.

It is not appropriate for issuers to take a blanket approach to the assessment of the status of the information they hold. Issuers should not consider that information to be included in periodic financial reports will always or never constitute inside information."

It is worth remembering that the test for being inside information has multiple elements:

- the information is of a "precise nature".
    - Information is of a precise nature if it:

    - Indicates a set of circumstances that exists or may reasonably be expected to come into existence, or an event that has occurred or may reasonably be expected to occur (*read: has a more than fanciful chance of occurring*); and
    - Is specific enough to enable a conclusion to be drawn on the possible effect of that set of circumstances or event on the prices of the financial instruments.

- The information relates, directly or indirectly, to one or more issuers or to one or more financial instruments.
- The information has not been made public.
- The information is likely to have a significant (*read: non-trivial*) effect on the price of the securities (reasonable investor test).

If PFI does constitute or contain inside information (which is for the issuer to determine), then delaying its disclosure will require the issuer to meet (and continue to meet throughout the delay period) the criteria to delay disclosure under MAR, keep the appropriate records and insider list and make the appropriate DDIIN when it is released.

The delayed disclosure criteria are:

- immediate disclosure is likely to prejudice the legitimate interests of the issuer
    - This may be satisfied by an issuer's need to manage the orderly release of information, complete audits and reviews etc. The FCA have recognised this in TN506.2 in relation to PFI and confirm that the FCA considers that cases where immediate disclosure of inside information is likely to prejudice the legitimate interests of an issuer include circumstances where:

      "*the issuer is in the process of preparing a periodic financial report and immediate public disclosure of information to be included in the report would impact on the orderly production and release of the report and could result in the incorrect assessment of the information by the public."*
    - Note that particular elements of PFI which may be inside information in and of themselves can (and should) be separately announced if there is an issue around fulfilling the other two delayed disclosure criteria in relation to those elements.
- Delay of disclosure is not likely to mislead the public
    - There are no exemptions available to this criterion. If withholding inside information will mislead the public, it must be released without delay.
    - Misleading situations include not releasing information which:
        - is materially different from the previously announced position.
        - details the fact that the issuer's financial objectives are not likely to be met, where such objectives were previously publicly announced.

        - is in contrast with the market's expectations, where such expectations are based on signals that the issuer has previously sent to the market, such as interviews, roadshows or any other type of communication organized by the issuer or with its approval.

- The issuer is able to ensure the confidentiality of the information.

Unscheduled Financial Information

In the FCA's review period, there were 3,132 trading statements released by issuers, but only 49 DDINs submitted to the FCA. The FCA noted that this may be due to timely release of inside information or could indicate a knowledge and compliance gap on the part of issuers. The FCA made clear that they consider it less likely that delayed announcement of these sorts of updates can be justified under MAR due to their very nature. Where delaying disclosure is likely to mislead the public, the information needs to be released without delay even if the issuer has a legitimate interest to protect and can keep the information confidential.

Issuers should routinely track and monitor their ability to deliver in line with market expectations using internal management information. Where there is reason to believe that there may be under or overperformance, immediate assessment of the position should be undertaken to determine whether inside information has arisen fulfilling the criteria set out above. It is possible that the necessary quality of precision may not arise immediately but even where an initial assessment does not result in a determination of inside information, the position should be kept under review and reassessed regularly as the situation develops. We recommend that issuers keep records of these assessments.

Significant unplanned events which meet the inside information criteria may also give rise to the need to announce and should be assessed as soon as possible.

Board Changes

The FCA reported that it was surprised by the number of notifications under this category given that ESMA did not include a specific legitimate interest in relation to it. We expect that issuers are considering this a negotiation situation and that until contracts are signed it is sensible not to announce due to the potential for the issuer's position to be compromised. We also consider that whether a board appointment would be considered inside or not would be very dependent on the specific post and the candidate. In any case, where a change to the Board is in contemplation, issuers should consider early on the potential for inside information to arise and how to manage that as the recruitment process develops.

Resignations should also be considered in the context of MAR.

Inside Information Management

The FCA note in their review that where issuers do not have adequate arrangements in place for the identification, handling and disclosure of inside information, this may place them at risk of unreasonably delaying disclosure or failing to prevent unlawful disclosure of inside information. Companies should review their procedures in light of the FCA's commentary, particularly around PFI, and consider whether any updating and/or training is appropriate.

Implications

It is worth bearing in mind that when a company is in possession of inside information, there will be implications for share dealing under its share dealing code and its ability to grant options during a closed period.

Summary

We advise that issuers include consideration of MAR early in the processes of preparing periodic financial information, undertaking a change to the Board and in all cases where the Company may be deviating from expectations and a trading update may be required, bearing in mind that the interpretation of the various elements of the inside information definition suggest lower trigger thresholds than a plain reading would suggest. With PFI, we suggest that this become a routine part of the internal reporting and review process. Where inside information assessments are undertaken but a decision is reached that information is not inside information, we recommend that this be documented.

We also recommend that companies review their inside information identification, management and disclosure processes to ensure that they are sufficiently robust and clear and consider the need for additional or periodic refresher training.

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