Recent FCA and English High Court Decisions Provide Guidance on Unlawful Disclosure of "inside information" and the Definition of PDMRs under UK MAR

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Introduction

Recent decisions by the Financial Conduct Authority (the "FCA") and High Court have provided some guidance on the scope of what constitutes unlawful disclosure of "inside information" and the definition of persons discharging managerial responsibilities ("PDMRs"), respectively. The FCA has also considered whether insiders are required to assess whether information is "inside information" even if the issuer has not made such a determination and whether having a relationship agreement or non-disclosure agreement in place would be sufficient to permit issuers to disclose "inside information" to their major shareholders before such information is released to the market. Separately, the High Court's ruling has provided insight on whether *de facto* directors and shadow directors fall within the scope of a PDMR.

We discuss these decisions in greater detail below.

Unlawful Disclosure of Inside Information

On 5 August 2022, the FCA issued a final notice imposing a financial penalty of £80,000 on Sir Christopher Gent ("CG"), the former non-executive Chair of ConvaTec Group Plc ("ConvaTec"), for unlawfully disclosing "inside information" in breach of Article 14(c) of the EU Market Abuse Regulation[1] ("EU MAR"), which has been transposed into the UK Market Abuse Regulation ("UK MAR"). As part of its decision, the FCA has provided important guidance on what it believes constitutes unlawful disclosure of "inside information".

Background

In October 2018, the ConvaTec board of directors, including CG, became aware that ConvaTec may not meet its previously published financial guidance following significantly reduced customer demand, which led ConvaTec's board to consider

[1] Regulation (EU) No 596/2014.

whether to issue a revision of its financial guidance to its investors. In light of these developments, on 10 October 2018, the CEO of ConvaTec informed CG that he was exploring potential retirement, subject to reaching an agreement with ConvaTec on remuneration and exit arrangements.

Later the same day, CG disclosed to two of ConvaTec's major shareholders that, subject to the analysis by the board of the revised financial forecasts, ConvaTec was planning to publish an RNS announcement on 15 October 2018 stating that it expected to revise its financial guidance and that ConvaTec's CEO would likely, in that case, be retiring. CG told the shareholders informed to keep the information confidential and to not trade on the basis of such information. The proposed updates were subsequently disclosed to the market via two RNS announcements released on 15 October 2018, resulting in ConvaTec's share price falling by 33.1% by market close that same day.

Decision

The FCA found that CG's conduct amounted to unlawful disclosure of "inside information" under Article 10 of EU MAR and a breach of the prohibition on the unlawful disclosure of "inside information" under Article 14(c) of EU MAR.[2]

Under Articles 7(1) and 7(4) of EU MAR, information will be deemed "inside information" if:

- the information is of a precise nature;
- the information has not been made public;
- the information relates directly or indirectly to one or more issuers or to one or more financial instruments; and
- if such information was made public, it would likely have a significant effect on the prices of such financial instruments.

Article 7(2) of EU MAR provides that information is of a precise nature if it concerns a set of circumstances which existed and/or an event which was reasonably expected to occur and it is specific enough for a conclusion to be drawn on the possible effects of such set of circumstances and/or event on the price of financial instruments.

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[2] The FCA's finding was made under EU MAR as, at the time of the events, EU MAR applied. Following the UK's exit from the European Union, the UK Market Abuse Regulation, which is substantially similar to EU MAR, now applies in the UK.

The FCA held that when CG made the disclosures to the two major shareholders on 10 October 2018, the information disclosed constituted "inside information" under Article 7 of EU MAR given that, at the time of such disclosures, there was a realistic prospect that both the financial guidance would be revised and the CEO would retire.

The FCA further stated that, given that CG received training with regards to EU MAR, and his experience and position, he had acted negligently in disclosing such information. CG should have known that the information would or might constitute "inside information" and that it was not in the normal exercise of his employment, profession or duties to disclose it. The FCA reached this conclusion notwithstanding the fact that at the time of disclosure: (i) ConvaTec had not yet determined that the information about the expected revision and the CEO's potential retirement is "inside information"; (ii) a ConvaTec executive and one of ConvaTec's brokers knew that CG was going to call the two main shareholders; and (iii) ConvaTec had a relationship agreement with one of the main shareholders which imposed confidentiality and no-dealing obligations, and CG made the disclosures with the express understanding that the individuals to whom he made the disclosures would keep the information confidential.

In finding against CG, the FCA stated that it was not reasonable and necessary for CG to disclose such information to certain of ConvaTec's major shareholders five days prior to the expected release of the RNS announcement. The FCA noted that this was contrary to ConvaTec's normal procedures, which was to hold such discussions only after the relevant RNS announcement had been approved after market close, on the evening, prior to such announcement, and that, to date, such discussions had been limited to those shareholders with whom ConvaTec had relationship agreements in place.

Comment

The FCA's decision provides useful guidance on what constitutes unlawful disclosure of "inside information" in two respects.

Firstly, the responsibility for determining what is "inside information". The FCA was not swayed by CG's argument that at the time CG made the disclosure, ConvaTec itself had not yet determined that the information constituted "inside information". The FCA concluded that as CG had prior training on EU MAR and due to his experience and position, he should have known that such information might constitute "inside information". Company executives cannot, therefore, rely on a company's assessment of whether the information constitutes "inside information" and they must make a determination themselves, particularly those with experience and in a senior position.

Secondly, the FCA rejected CG's argument that he was entitled to reach out to certain large shareholders to give them an early warning that the announcement was coming,

given the imposition of confidentiality under the relationship agreement with one of the shareholders informed and that he had told the recipients to keep the information confidential and not to trade on the information. While DTR 2.5.7G(2) provides that an issuer may, depending on the circumstances, be justified in disclosing "inside information" to certain categories of recipients, including major shareholders, the FCA clarified that any such disclosure of "inside information" must be "reasonable and necessary" to be permitted. The FCA's decision has clarified that issuers and insiders may not disclose "inside information" to major shareholders well before a planned announcement, even if those shareholders are subject to non-disclosure restrictions and no-trading undertakings. While the FCA did not expressly approve ConvaTec's internal policy, the decision implies that the FCA may consider the disclosure of "inside information" by issuers to its major shareholders the night before (once the markets have closed) such information is to be released to the market as reasonable and necessary for the purposes of MAR, so long as appropriate measures are in place to ensure that the recipients are aware of the confidential nature of such information and undertake not to trade on it.

The Scope of Who Is a PDMR

In *Allianz Global Investors GmbH and others v G4S Limited (formerly known as GS4 PLC) [2022] EWHC 1081 (Ch)* ("Allianz"), the High Court ruled that the definition of PDMRs in paragraph 8 of Schedule 10A of the Financial Services and Markets Act 2000 ("FSMA") includes *de facto* directors and, potentially, even shadow directors of a company for the purposes of claims made under section 90A (liability of issuers in connection with published information) of FSMA.

Background

The claimants, all of whom were institutional shareholders of G4S, whose subsidiary provided services to the Ministry of Justice for the electronic monitoring of prisoners pursuant to various contracts, issued three claims against G4S alleging that information provided by the defendant to the market contained untrue and misleading statements, or omitted material information and that there was dishonest delay in its publishing.

The claimants argued that there were five individuals within G4S or its subsidiary that were PDMRs and that had knowledge, or were reckless as to, the inaccuracy and misleading nature of the published information. Four of these individuals were *de jure*[3] directors of the subsidiary of G4S, but not on the board of G4S itself. The defendant

[3] That is a statutory director, legally appointed to the board of the company.

applied for strike out or summary judgment on the grounds that the directors were not *de jure*, *de facto*[4], or shadow directors of G4S.

Decision

Section 90A of FSMA, which concerns the liability of issuers of securities to pay compensation to persons who have suffered a loss as a result of a misleading statement or dishonest omission in certain published information relating to the securities or a dishonest delay in publishing such information, states that the operative provisions are to be found in Schedule 10A, paragraph 8(5) of which states that:

"For the purposes of this Schedule the following are persons 'discharging managerial responsibilities' within an issuer –

- *any director of the issuer (or person occupying the position of director, by whatever name called);*
- *in the case of an issuer whose affairs are managed by its members, any member of the issuer;*
- *in the case of an issuer that has no persons within paragraph (a) or (b), any senior executive of the issuer having responsibilities in relation to the information in question or its publication."*

The court rejected the claimants' submission that the statutory definition of PDMR included "senior executives responsible for managerial decisions affecting the future developments and business prospects of the issuer and/or those business units", instead finding that the definition in paragraph 8(5) of Schedule 10A was "clear and unambiguous" and should be given its "natural meaning". However, the court also rejected the defendant's application for strike out and summary judgment, confirming that the definition of PDMR includes not only formally appointed *de jure* directors, but also shadow directors and *de facto* directors, and that the claimants had a real prospect of demonstrating at trial that G4S' subsidiary directors were *de facto* directors of G4S.

Comment

The court's decision provides important guidance on the UK's PDMR regime and potentially expands its scope. The determination of whether an individual is a *de facto* director is ultimately a factual question, and issuers should therefore consider, based on a detailed factual assessment taking into consideration their governance structure, whether there is anyone in their organisation that participates in the decision-making of

[4] That is acting as a director, but not legally appointed to the board.

the issuer's board, as any such individual could be considered to be a *de facto* director or shadow director and, therefore, a PDMR for the purposes of section 90A and Schedule 10A of FSMA.

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Please do not hesitate to contact us with any questions.

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