ALERT MEMORANDUM

Italy Strengthens Criminal Sanctions Against Market Abuse and Amends the Rules on Confiscation

February 3, 2022

On February 1, 2022, Law No. 238 of December 23, 2021 concerning "*Provisions for the fulfilment of the obligations arising from Italy's membership of the European Union - Europe Law 2019-2020*", published in the Official Gazette on January 17, 2022 (the "**Europe Law**"), entered into effect. The Europe Law, among other things, amends the provisions against **market abuse** .

In particular, Article 26 of the Europe Law amends the penalties set out in the Consolidated Finance Act (Legislative Decree No. 58 of February 24, 1998, the "**TUF**").

Among the most salient provisions, the Europe Law:

- strengthens the criminal sanctions against so-called "*primary insiders*";
- introduces a specific criminal sanction against so-called "*secondary insiders*";
- limits the applicability of mandatory confiscation set out in Article 187 TUF to the profit deriving from the offense (which no longer extends to the product and the means used to commit it).

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1. The amendments to the market abuse rules

The main amendment introduced by Article 26 of the Europe Law concerns the offense of insider dealing (Article 184 TUF), which can also entail corporate liability pursuant to Article 25-*sexies* of Legislative Decree No. 231 of June 8, 2001 ("**Decree 231**").

In particular, the Europe Law changes Article 184 TUF by:

- **amending** the heading of the new Article 184 TUF, renaming it "*Abuse or unlawful disclosure of inside information. Recommendation to or inducement of others to commit insider dealing*";[1]
- **strengthening sanctions against the so-called primary insider**, i.e. the person who is aware of inside information "*by virtue of (i) his/her membership of administrative, management or supervisory bodies of the issuer, or (ii) his/her holding in the issuer's capital, or (iii) the exercise of a working activity, of one or more functions, also public, or of an office*", and against the so-called criminal insider, *i.e.*, the person who has inside information "*by reason of the preparation or execution of criminal activities*". The current penalty of imprisonment from one to six years is raised to a minimum of two years and a maximum of twelve years of imprisonment, together with a fine ranging from EUR 20,000 to EUR 3 million;
- **introducing criminal liability of the so-called secondary insider**, *i.e.*, the person in possession of inside information for reasons other than those mentioned above, who may be subject to imprisonment from one year and six months to ten years and a fine ranging from EUR 20,000 to EUR 2.5 million, except in cases of complicity in the offense of the primary insider (which is punished with the same penalties applicable to the primary insider);
- **extending also to secondary insiders the aggravating circumstance set out in Article 184(3) TUF,** which provides for an increase of the fine up to three times or up to the greater amount of ten times the product or the profit derived from the offense, when, due to the seriousness of the actions, the personality of the offender or the entity of the mentioned product or profit, even the maximum basic fine appears to be inadequate;
- **introducing a new paragraph 5** providing for the application of the offense of insider dealing also to conduct or transactions relating to "*auctions on an authorized auction platform, such as a regulated market for emission allowances or other related auctioned products, even where the auctioned products are not financial instruments*".

The Europe Law also impacts other market abuse provisions, in particular by:

- amending the scope of the criminal offenses and the administrative violations provided in the TUF (which is extended, for example, to credit default swaps and differential contracts);
- including "*securities or associated instruments*" - as defined by the European Market Abuse Regulation of April 16, 2014[2] - among those exempt from the penalties, "*when such negotiations are carried out in accordance with Article 5(4) and (5) of the abovementioned European Regulation*"[3];

[1] Previously, Article 184 TUF was simply named "*Insider dealing*".

[2] Pursuant to Article 3(2)(a) and (b) of Regulation (EU) No. 596/2014 on market abuse ("MAR"), "*securities*" means "*(i) shares and other securities equivalent to shares; (ii) bonds and other forms of securitized debt; or (iii) securitized debt convertible or exchangeable into shares or into other securities equivalent to shares*", while "*associated instruments*" means "*the following financial instruments, including those which are not admitted to trading or traded on a trading venue, or for which a request for admission to trading on a trading venue has not been made: (i) contracts or rights to subscribe for, acquire or dispose of securities; (ii) financial derivatives of securities; (iii) where the securities are convertible or exchangeable debt instruments, the securities into which such convertible or exchangeable debt instruments may be converted or exchanged; (iv) instruments which are issued or guaranteed by the issuer or guarantor of the securities and whose market price is likely to materially influence the price of the securities, or vice versa; (v) where the securities are securities equivalent to shares, the shares represented by those securities and any other securities equivalent to those shares*".

[3] The reference is to the MAR. In particular, the prohibitions on insider dealing and market manipulation do not apply to "*trading in securities or associated instruments for the stabilization of securities*" where: *"(a) stabilization is carried out for a limited period; (b) relevant information about the stabilization is disclosed and notified to the competent authority of*

- **limiting the scope of the mandatory confiscation to the profit derived from the offenses** of insider dealing and market manipulation. The confiscation of the product and the means used to commit the abovementioned offenses is no longer contemplated.

2. The liability of secondary insiders

The introduction of a criminal sanction against secondary insiders is, without doubt, one of the most significant amendments made by the Europe Law. Indeed, Law No. 62/2005, by repealing the criminal sanction previously provided against secondary insiders[4], had transformed their conduct from a criminal offense to an administrative violation, although with particularly onerous fines[5].

Therefore, until now, the TUF distinguished between the unlawful exploitation of inside information carried out by a primary insider - which constituted a criminal offense under Article 184 TUF - and the same unlawful conduct carried out by a secondary insider, subject only to an administrative sanction under Article 187-*bis* TUF.

However, the secondary insider could also be subject to the criminal sanctions laid down in Article 184 TUF, in cases of complicity in the offense of the primary insider (namely, where he/she had knowingly aided the primary insider in the commission of the offense). In short, until now, the secondary insider could be subject to: (a) a mere administrative sanction under Article 187-*bis* TUF, if he/she had exploited inside information for his/her own exclusive benefit, or (b) the criminal sanction provided in Article 184 TUF, in cases of complicity in the offense of the primary insider.

The Europe Law introduces once again the criminal liability of the secondary insider. However, the secondary insider will be punished with a less severe sanction than the one provided against the primary insider. The secondary insider will be punished, if:

a) he/she has obtained the inside information for reasons other than those of the primary insider;
b) he/she is aware of the privileged nature of such information, regardless of its source.

This without prejudice to the application to secondary insiders of the more serious sanction provided against primary insiders (Article 184(1) TUF), in cases of complicity with them.

3. The amendments to the rules on confiscation

Another significant amendment was made to the confiscation rules set out in Article 187 TUF. This provision, in its previous formulation, provided for the mandatory confiscation of the product or profit of the offense and of the means used to commit it, in cases of conviction for the offenses of insider dealing and market manipulation. This measure, which had been severely criticized for being excessive, led to the confiscation of large sums of money, including, for example, shares and securities used to commit the insider dealing offense.

With the entry into effect of the Europe Law, the confiscation under Article 187 TUF is now limited only to the profit[6].

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the trading venue in accordance with paragraph 5; (c) adequate limits with regard to price are complied with; and (d) such trading complies with the conditions for stabilization laid down in the regulatory technical standards referred to in paragraph 6".

[4] The original Article 180 TUF (prior to the reform introduced by Law No. 62 of April 18, 2005) provided for a criminal sanction both against the primary and the secondary insider who had obtained the privileged information from the former.

[5] On the "punitive" nature of the administrative sanctions provided in the TUF and on the extension of the safeguards granted in the context of the relevant administrative procedures see also *Constitutional Court: greater safeguards against "punitive" administrative penalties* and *Market Abuse: The Court of Justice of the European Union recognizes the right to remain silent before CONSOB*.

[6] This amendment is in line with Judgment No. 112 of March 6, 2019 of the Italian Constitutional Court, which declared unconstitutional the mandatory confiscation of the product and assets used to commit the violations set out in the TUF with reference to those punished with an administrative sanction (Article 187-*sexies* TUF).