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Market Abuse Regulation: Impact on U.S. Public Companies—Part I

*Raj S. Panasar, Aseet Vasudev Dalvi, Jackson Martin, Leslie N. Silverman and Sandra L. Flow**

This multi-part article focuses on the Market Abuse Regulation's implications for U.S. public companies' ongoing obligations and other ordinary course activities if they have debt, equity or other securities admitted to trading on EU trading venues, or are contemplating such admissions to trading. This first part of the article gives an overview of the changes made to the previous regime by the Market Abuse Regulation, with particular focus on the ongoing obligation to disclose inside information. The final parts of this article, which will appear in upcoming issues of The Banking Law Journal, *will focus on restrictions on managers' dealings, the obligation to maintain insider lists and impacts on share repurchase programs, as well as certain other considerations.*

The Market Abuse Regulation ("MAR"), which entered into force on July 3, 2016, has required U.S. public companies with debt, equity, or other securities admitted to trading on EU regulated markets or "multilateral trading facilities," or contemplating such admissions to trading, to devote considerable effort to assessing and preparing to comply with the new EU-wide market abuse regime.

For most companies, the most relevant MAR requirements for their ongoing obligations and ordinary course activities will be those that relate to ongoing disclosure of "inside information," managers' transactions, insider lists and share repurchases.

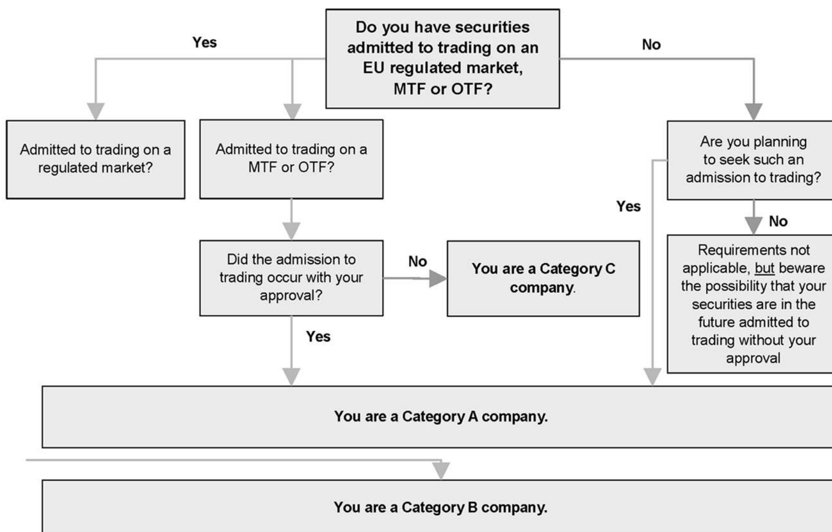
The significance of these requirements to U.S. public companies, and the work necessary to comply with them, are likely to differ based on which of the following three categories these companies fall into (which, for purposes of this article, we style as Categories A, B, and C, in order of magnitude of expected impact):

- Category A—highest impact—companies whose debt, equity or other

* Raj S. Panasar (rpanasar@cgsh.com) is a partner at Cleary Gottlieb Steen & Hamilton LLP focusing his practice on international financing transactions. Aseet Vasudev Dalvi (adalvi@cgsh.com) is an associate at the firm focusing his practice on international capital markets transactions. Jackson Martin (jamartin@cgsh.com) is an associate at the firm concentrating his practice on international corporate and financial transactions. Leslie N. Silverman (lsilverman@cgsh.com), a partner at the firm, focuses his practice on domestic and international capital markets, representing both issuers and underwriters. Sandra L. Flow (sflow@cgsh.com) concentrates her practice on capital markets and corporate governance.

securities are *not* currently admitted to trading on an EU regulated market,[1] but are admitted to trading on other EU trading platforms (*i.e.*, MTFs or OTFs)[2] *with* those companies' approval, or that are contemplating any such admission to trading;

- Category B—medium but significant impact—companies whose debt, equity or other securities are currently admitted to trading on EU regulated markets; and
- Category C—lowest but potentially significant impact—companies whose debt, equity or other securities are (or in the future become) admitted to trading on MTFs (or OTFs) *without* their approval.



An additional, and potentially overarching, consideration for Category A and B companies assessing the implications of MAR relates to *which* of their securities are admitted to trading in the EU. Article 2 of MAR, its "scope"

[1] EU regulated markets, broadly, include the main platforms of the EU stock exchanges.

[2] "Multilateral trading facilities" or "MTFs" are financial trading platforms that are not traditional stock exchanges, including a number of popular trading venues like the Euro MTF in Luxembourg, the Global Exchange Market in Ireland, the Alternative Investment Market in the UK and the Open Market of the Frankfurt Stock Exchange. "Organised trading facilities," or "OTFs," are a new category of trading venue introduced by MiFID II for bonds, structured finance products, emission allowances and derivatives. OTFs are similar to MTFs, but the execution of orders is carried out by the OTF operator in a discretionary way. MAR will only apply to OTFs from January 3, 2018.

provision, expressly applies the regulation only to:

- financial instruments admitted to trading on EU regulated markets, MTFs or OTFs (or, in the case of regulated markets or MTFs, for which admission to trading has been requested); and
- financial instruments whose price or value depends or has an effect on the price or value of those EU-traded securities.

Thus, although a U.S. public company with only straight debt (*i.e.*, non-convertible debt) admitted to trading in the EU with its approval will be subject to the full range of MAR requirements, the text of MAR's scope provision supports the view that the requirements should generally only apply to, and be understood only in the context of, those debt securities admitted to trading in the EU (and other securities with a price-value relationship with those debt securities, if any). Conversely, for a U.S. public company with a secondary equity listing in the EU that has no debt admitted to trading in the EU, the text of MAR's scope provision supports the view that MAR requirements generally should *not* apply to its outstanding debt (absent a price-value relationship with the equity).

Regulators' views on MAR's scope continue to evolve, however, and we understand that at least one EU competent authority appears to be taking the position that at least some of MAR's requirements apply to *all* of a company's securities if it has *any* securities admitted to trading in the EU, although that view has not been formally expressed. Nevertheless, at this time, it seems reasonable to comply with MAR's requirements as laid out in its scope provision, particularly given the burden of extending MAR's requirements to all of a company's securities, whether or not admitted to trading in the EU. However, U.S. public companies should closely monitor developments in the relevant member state(s) in which their securities are admitted to trading for formal guidance on this issue.

CATEGORY A—HIGHEST IMPACT
Category A companies were not previously subject to Market Abuse Directive ("MAD") requirements and, generally, are not subject to any analogous requirements under MTF rules. For these companies, MAR represents a sudden plunge into the EU market abuse regime and its requirements, superimposing a new layer of regulation on the existing framework to which they are subject under the U.S. Securities Exchange Act of 1934 (the "Exchange Act"), the U.S. Sarbanes-Oxley Act of 2002 and the rules of the Securities and Exchange Commission (the "SEC") and the U.S. stock exchanges. In particular, these companies:

- have now become subject to a material event reporting regime that is premised on a general obligation to disclose *all* "inside information" (a concept similar to material non-public information under the U.S. federal securities laws, although potentially broader) to the market *as soon as possible*, which may require disclosure of more information, and earlier, than would be required under Form 8-K;
- have, together with directors and certain senior employees (and certain associated persons), now become subject to a new transaction reporting regime that in many respects is broader than section 16 of the Exchange Act—extending to a potentially wider range of securities (for example, debt securities, although the securities covered may reasonably be limited to the company's securities that are admitted to trading in the EU and any securities that have a price-value relationship with those securities) and transactions (including pledging and lending) and imposing direct reporting obligations not only on directors and senior employees, but also on associated persons and public companies themselves;
- will now have their directors and certain senior employees made subject to new prescribed "closed periods" (30 calendar days before the publication (through prescribed channels, where applicable) of an interim financial report or a year-end report), which may limit the ability to use Rule 10b5-1 plans and potentially restrict trading windows, although the securities covered again may reasonably be limited to the company's securities that are admitted to trading in the EU and any securities that have a price-value relationship with those securities;
- are now required to maintain lists of all persons who have access to inside information in a prescribed, detailed format, which may entail a significant diligence burden;
- may face new restrictions on share repurchase programs; and
- have become subject to EU prohibitions on insider dealing, unlawful disclosure of inside information and market manipulation.

For these companies, the burden of becoming familiar with, assessing the impact of, and implementing policies, procedures and practices to comply with MAR has been and will continue to be particularly keenly felt. Indeed, in light of the additional burden and costs of compliance, some U.S. public companies with securities listed only on an MTF or OTF may wish to consider the possibility of delisting or migrating the listing of those securities.[3]

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[3] Delisting, however, may have adverse consequences for some companies. For instance, a U.S. public company may wish to maintain an EU listing for debt securities, for example, to preserve a diverse base of European investors (investment mandates of which frequently require investments in listed instruments), for tax reasons or to retain eligibility for the European Central Bank's asset purchase program (which is being extended to include purchases of corporate debt). Many companies also maintain EU listings to facilitate employee share incentive plans.

CATEGORY B—MEDIUM BUT SIGNIFICANT IMPACT[4]
Category B companies should already have had procedures in place to comply with MAD, as implemented in the relevant member state(s) in which their securities are admitted to trading. For these companies, many aspects of the new regulatory regime will be familiar, and changes necessitated by MAR may primarily be procedural. Even for these companies, however, the possibility that MAR (many aspects of which remain subject to significant interpretive uncertainty) entails meaningful new substantive restrictions and requirements should not be lightly dismissed. This is particularly true as concerns: • the extent to which inside information must be identified and segregated in announcements and website disclosures; and • the doubtful ability to continue to make use of even fully discretionary Rule 10b5-1 compliant trading plans during new prescribed closed periods and the potential impact of those closed periods on directors' and senior employees' trading windows (although the securities covered may reasonably be limited to the company's securities that are admitted to trading in the EU and any securities that have a price-value relationship with those securities). Category B companies with only listed debt, however, have not previously been subject to MAD's transaction reporting requirements, and, for these companies and their directors and senior employees (and certain associated persons), compliance with the reporting regime may represent more of an incremental burden (although the securities covered again may reasonably be limited to the company's securities that are admitted to trading in the EU and any securities that have a price-value relationship with those securities).

CATEGORY C—LOWEST BUT POTENTIALLY SIGNIFICANT IMPACT[5]

[4] In contrast to MAD, which was subject to relevant implementing measures in each member state, MAR is a "maximum harmonization" regulation, and EU competent authorities are prevented from retaining rules, evidential provisions or guidance that conflict with it. For Category B companies already subject to MAD, any assessment of MAR's incremental burden will necessarily entail an analysis against MAD as implemented in their relevant member state(s).

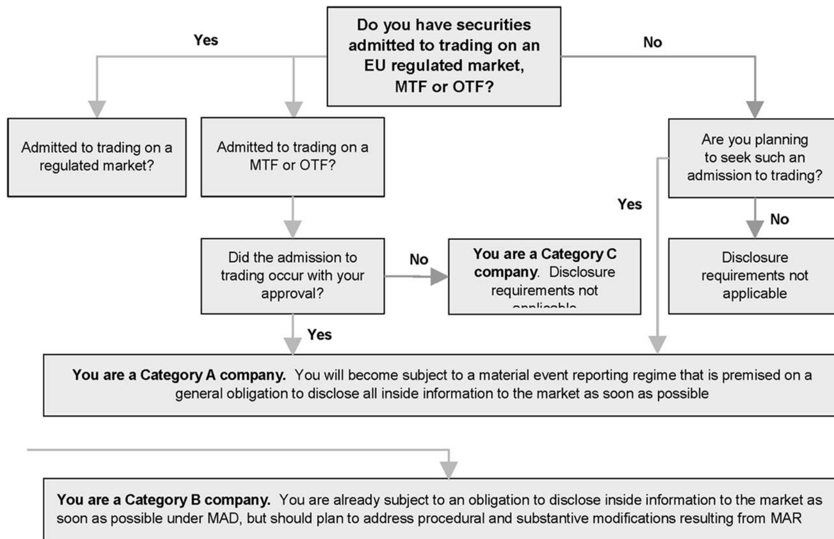
[5] U.S. public companies may ask how to determine whether their securities have been admitted to trading on an MTF or OTF without their approval. One preliminary reference point will be the website of the European Securities and Markets Authority ("ESMA"), where ESMA currently maintains a register of shares admitted to trading on regulated markets, which will be expanded to cover all securities admitted to trading on regulated markets, MTFs or OTFs.

Category C companies, whose securities are admitted to trading on an MTF or OTF without their approval, are generally only subject to MAR's prohibitions against insider dealing, unlawful disclosure of inside information and market manipulation. Accordingly, MAR's impact on their ongoing obligations and ordinary course activities is likely limited. Nevertheless, in view of MAR's potential extraterritorial reach, even Category C companies should familiarize themselves with the safe harbor for share repurchase programs and update compliance manuals and training programs to incorporate relevant MAR prohibitions.

The remainder of this article analyzes MAR's impact on U.S. public companies in further detail. The sections have been organized thematically and are preceded by flowcharts that summarize the general impact on Category A, B, and C companies. The Annex to this article provides an additional tabular summary comparing relevant MAR requirements, their evolution from MAD (as implemented in the UK), and the U.S. regulatory backdrop applicable to U.S. public companies.

Note that while this article addresses the impact of MAR primarily for domestic U.S. public companies, much of the discussion will also be relevant to non-EU "foreign private issuers" that are subject to portions of the broader U.S. regulatory regime and that, because of present or future admissions to trading on EU trading platforms, will also be affected by MAR.

ONGOING DISCLOSURE OF INSIDE INFORMATION (*Category A and B Companies*)



MAR (like MAD, but see further discussion below) requires companies to publicly disclose "inside information" that directly concerns them "as soon as possible." Inside information must be disseminated in a manner that "enables fast access and complete, correct and timely assessment of the information by the public." It must also be posted on the company's website and maintained there for five years. As was the case under MAD, a company may delay disclosure of inside information to protect its "legitimate interests," provided that the delay is unlikely to mislead the public and confidentiality can be maintained.[6]

Category A companies primarily accustomed to the Form 8-K regime may now need to disclose more information to the market and more rapidly than they otherwise might have, both because "inside information" may extend to types of information that are not reportable events under Form 8-K and because the deadline for disclosure is earlier than the four business day timeframe that Form 8-K generally requires. For these companies, compliance with the basic premise of the EU reporting regime—continuous reporting of *all* inside information *as soon as possible*—may, depending on what securities are admitted to trading in the EU (as discussed further below), require meaningful updates to disclosure controls and procedures and, to some extent, a shift in mindset.

[6] For companies that are financial institutions or credit institutions, MAR adds another basis for delay: delay in order to preserve the stability of the financial system.

The more notable points for Category B companies (and also key points for Category A companies to consider in assessing differences from their SEC reporting obligations) are likely the following:

- *Potentially wider definition of "inside information"*: MAR defines inside information as "information of a *precise nature*, which has not been made public, relating, directly or indirectly, to one or more issuers or to one or more financial instruments, 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*" (emphasis added). It further provides, however, that information that "would be likely to have a significant effect on . . . pric[e]" means information that a "reasonable investor would be likely to *use* as *part of the basis* of his or her investment decisions."

  This reasonable investor test is potentially very broad. In contrast, under the U.S. federal securities laws, information will not generally be viewed as "material" absent a *substantial likelihood* that a reasonable investor would have considered it *important* in making an investment decision, and that case law formulation is situated against the backdrop of judicial guidance that makes clear that the formulation was intended, among other things, to avoid subjecting investors to "an avalanche of trivial information."[7] Further, under the test in MAR, the relevance of the likely effect of disclosure on price (on which the test in MAD turned) is unclear,[8] whereas in the U.S. context, the impact of disclosure on market price, though not determinative, is clearly recognized as a factor to be taken into account in an assessment of

[7] *TSC Industries, Inc. v. Northway, Inc.,* 426 U.S. 438, 96 S.Ct. 2126, 48 L.Ed.2d 757 (1976).

[8] It should be noted that the equating (within MAR itself) of the concept of likely significant effect on price with the concept of whether a reasonable investor would be likely to use the information represents a subtle shift from MAD. Under the MAD regime, although an essentially identical reasonable investor test was set out in an EU implementing directive (and there too was framed as the definition of what constitutes a likely significant effect on price), guidance from the Committee of European Securities Regulators ("CESR") made clear that the reasonable investor test was merely intended to "*assis[t]* in determining the type of information to be taken into account" in assessing a likely significant effect on price. Moreover, since MAD itself precluded implementing measures (in this case, one setting forth the reasonable investor test) from modifying the essence of a MAD provision (in this case, the requirement of a likely significant effect on price), interpretations that sought to reconcile the price-sensitivity and reasonable investor tests by deemphasizing the likely effect of disclosure on market price were always questionable. Under MAR, in contrast, there is greater uncertainty as to whether the likely effect of disclosure on market price remains part of the analysis.

materiality.

In light of the above, and the practical reality that the adequacy of particular disclosures will be assessed by courts and regulators with the benefit of hindsight, U.S. public companies with equity admitted to trading on EU trading venues (or any other securities with a price-value relationship with equity, like convertible debt) in particular would be well advised to take a conservative approach to their disclosure choices (as they should, in any event, in complying with U.S. law).

Companies with only straight debt admitted to trading in the EU should, in general, find the EU continuous reporting obligation less burdensome since any determination of whether information comprises inside information in the debt context would appropriately focus on the relevance of the information to a debt investor (including, for example, whether it is information that might affect credit ratings or creditworthiness). Still, in view of the potential breadth of MAR's reasonable investor test and the reality noted above that disclosure choices are often judged in hindsight, even the effectively higher disclosure bar in the debt context may represent a MAR risk that U.S. public companies should take into consideration.

- *Need to identify / label inside information as "inside information"*: In a change from MAD, implementing technical standards published by ESMA under MAR require that public disclosure of inside information be "clearly identif[ied]" as such. In practice, it is often the case that companies disclose information out of prudence because it *might* be inside information, without definitively concluding that it *is*, and a requirement to draw concrete conclusions at the point of each disclosure, and to label disclosed information accordingly, sets a potentially unhelpful precedent when making future disclosure choices. It may be that in certain EU member states, regulators will eventually permit slightly less precise formulations with respect to identification, such as a statement that a given announcement "includes" or "contains" inside information. This may mitigate, to an extent, but not entirely address, the concern.[9]

In light of this concern, it remains to be seen whether market practice

[9] For example, we understand that at least one competent authority has noted in informal discussions that it regards a general label of "may contain inside information" as non-compliant with MAR, and is currently considering whether a general label of "contains inside information" is acceptable on an announcement of any length.

will move in the direction of identifying disclosures as inside information except in the clearest cases. Where a definitive conclusion that information constitutes inside information cannot be reached, and disclosure is being provided as a matter of prudence or good practice, an unlabeled announcement, possibly coupled with disclaimers on the relevant section of the website that such portion of the website "includes" or "contains" (or may include or contain) inside information, may be a reasonable middle ground. However, in the absence of EU-wide guidance, it would be prudent for companies to monitor market practice and regulatory guidance in the relevant EU member state(s) in which their securities are admitted to trading.

- *Website segregation requirement*: ESMA's implementing technical standards require the inclusion of inside information in an "easily identifiable" section of the website, with clear indication of date and time of disclosure and organization in chronological order. The "easily identifiable" requirement represents a relaxation from an earlier ESMA proposal that would have required posting on a section of the website that "only" contained inside information, and appears to have been intended to permit companies to continue to use customary investor relations websites for these postings. MAR requires, however, that a company's disclosure of inside information must not be combined with "the marketing of its activities," while providing little guidance as to what marketing activities comprise. In the absence of guidance, it would be prudent for companies to review the investor relations sections of their websites and to remove, at a minimum, product advertisements and overly bullish text on the webpage itself, as well as any other posted materials of a sort not routinely included on investor relations websites that may be construed as being of a "marketing" nature.
- *Additional flexibility to delay disclosure, but also heightened scrutiny*: Although the basic criteria to delay disclosure of inside information (discussed above) have not changed under MAR, ESMA has published examples of "legitimate interests" that broaden the list of potential legitimate interests from those that have been recognized to date and provided examples of instances where delay would mislead the public.[10]

[10] The list of legitimate interests includes the following instances: where negotiations are in progress; where the company's financial viability is in grave and imminent danger; where the inside information is subject to the approval of another internal body of the company; where intellectual property rights might be jeopardized; where the inside information involves the

The additional flexibility to delay, however, has come with additional procedural burdens. Any decision to delay disclosure under MAR (in contrast to MAD) must be notified to the relevant competent authority at the time the relevant inside information is made public, and each competent authority may require the company to give reasons for the decision to delay disclosure, either as a matter of course or upon request. These new notification requirements will likely also increase regulatory scrutiny of delay decisions. Companies are now obliged to keep proper records about any decision to delay, including when the inside information first arose, when the decision to delay was taken, evidence of the satisfaction of the MAR requirements for delayed disclosure, the identity of the person(s) responsible for the decision to delay and other details specified in ESMA's technical standards. Companies that have not already done so will accordingly need to review their pre-MAR policies, procedures and practices to ensure that proper records are maintained.

Key Next Steps—Category A Companies
To the extent not already implemented: • Establish internal policies, procedures, and practices to, among other things: ○ identify inside information and disclose it as soon as possible through appropriate channels; ○ consider the appropriateness of delaying disclosure; ○ meet recordkeeping / notification obligations in connection with delayed disclosure; ○ label inside information appropriately at the time of announcement; and ○ retain inside information on your website for at least five years. • Review the investor relations section of your website and consider any needed updates to remove "marketing" materials; and • Institute necessary training programs for relevant staff.

Key Next Steps—Category B Companies
To the extent not already implemented: • Update internal policies, procedures, and practices to, among other things: ○ reflect a changed definition of "inside information";

buying or selling of major holdings in another entity; and where public authority approval is pending. Examples provided of instances where delay would mislead the public include: information that is materially different from a previous announcement; information that relates to the fact that previously announced financial objectives will not be met; and information that is in contrast to the market's expectations if those expectations are based on signals previously given by the company.

- ○ reflect new flexibility to delay disclosure (bearing in mind potentially heightened scrutiny of decisions to delay);
- ○ meet new recordkeeping / notification obligations in connection with delayed disclosure;
- ○ label inside information appropriately at the time of announcement; and
- ○ retain inside information on your website for at least five years (versus one year under MAD).
- Review the investor relations section of your website and consider any needed updates to remove "marketing" materials; and
- Institute necessary training programs for relevant staff.

* * *

The final parts of this article (including the Annex) will appear in upcoming issues of *The Banking Law Journal*.