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RETHINKING THE LEGAL CONCEPT OF INSIDER TRADING IN NIGERIA: CRITICAL ANALYSIS

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ABSTRACT

The concept of "insider trading or dealing" is a direct product of commercial activities in the area of securities exchange which is adequately provided for or regulated by statute. In this paper, we have made an attempt at critically examining the concept of "Insider Trading"– which involves trading in securities such as shares, debentures stocks bonds or debt securities. This paper critically examine the implication of insider dealings in lines with statutory provisions and case law as it affect false or misleading statement, fraudulently inducing person to deal in securities, prohibition of dealing in securities by insiders, abuse of information obtained in official capital, false trading, market rigging transaction securities and market manipulation. This paper is concluded with the necessaries remedies available to the victim and also recommends the

Introduction:

The concept of trade[1] involves the exchange of goods or services for money or other goods. Trade is a concept which is determined by profit and loss.

In this paper, we have made an attempt at critically examining the concept of "Insider Trading[1]"– which involves trading in securities such as shares, debentures, stocks bonds or debt securities.

Generally, as well as legally, the term speaks of a situation "where an individual or organization buys or sells securities while knowingly in possession of some piece of

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review of the provision of the Investment and Securities Act as compare with the England or UK insider dealing statutory provision, the Financial Securities and Market Act (FSAMA) 2000, part VIII, and others.

Keywords: *Rethinking, Legal Concept, Insider, Trading, Critical Analysis.*

Confidential, as well as "Price Sensitive[1] Information" which is not generally available and which is likely, if made available to the general public, to materially affect the price of these securities.

From the above, it can be gleaned that information is an important aspect of "trade and such information may form the basis for loss or profit in business, at the expense of one trader and to the advantage of the other. It is on this wise that the law seems to regulate the use of information obtained by a person with special privileges or relationship with the sources of that information which may determine the outcome of a trade in s securities market.

WHAT IS INSIDER TRADING?

The concept of "insider trading or dealing" is a direct product of commercial activities in the area of securities exchange which is adequately provided for or regulated by statute.[15]

The, term has described in the following manner.

"Insider dealing (or trading) occurs when a person in possession of price – sensitive information about a company buys or sells securities in that company and so obtains better terms in the contract of sale than would have been the case had the counterparty been aware of the information in question. In that way, the insider can either make a profit or avoid a loss,

[15] In Nigeria, see generally the provisions of section 105 to 116 of the investments and securities Act (ISA) 2007. For England, see the company Securities (insider Dealing) Act 1985, and the criminal justice Act 1993, part v.

depending on whether the information, once public, will drive the share price up or down".[16]

Therefore, once shares become easily bought and sold on a stock exchange the potential for those inside or connected to the company to abuse their knowledge of the company's future plans or announcements[17] arises. It is for this reason that every country in the world with a major stock exchange has made this practice illegal because of its potential to destroy public confidence in the stock exchange.

Thus in the same vein, having regard to the continuing obligations of companies and securities dealers, the statutes of various countries also try to ensure that opportunities for insider dealing are minimized by making necessary provisions to the effect that companies disclose any significant information that might affect share price as quickly as possible.

It is also worthy of note that insider dealing is not confined to securities issued by companies, but can equally occur in the market for government bonds.[18]

More often, "Insider Trading" is seen to be commercially immoral,[19]and morally reprehensible behavior[20] which gives the insider an unfair advantage over other investors.

INSIDER TRADING AT COMMON LAW

The case of *Percival v. Wright (1902)* forms the basis for the Common Law position. In that case, shareholders offered to sell shares to directors who

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16 Gower and Davies, *principles of modern company law*. .Eight Edition (London, Sweet& Maxwell 2008) 1083-4.

17 Alan Dignam and John Howry. Company Law fifth Edition (London, oxford University press 2009) 777

18 One of the earliest cases on market manipulation occurred in the market for government bonds .in *R v.* De Beranger (1814)3 M & S 68 the fraudster pretended to be solder returning from France with news of the defeat of Napoleon (before this event actually came to pass). The false rumors which they spread caused the price of British government bonds to rise, thus enabling the Accused to dispose of their holdings at a profit. (Gotten from Gower

19 Nutshells, *Company Law in a Nutshell Second Edition* (London Sweet & Maxwell 1992)25

20 Ibid. Alan & John 77

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knew their true value was greater because of an impending take – over bid, which information their confidential obligations to the company forbade them to disclose.

For that reason it was decided that the shareholder could not rescind the contract the directors had no general duty to the shareholders to disclose price-sensitive information to them. In the United States, the above rule has been circumvented by extending the categories of "special circumstances" requiring disclosed. (This is not the case for the English Courts) Although it was held in *Allen v. Hyatt* (1914) that directors exercising options to buy members' shares granted prior to merger should account to those members for profits made, since in negotiating the sale of the shares to the take – over bidder they were acting as members' agents.

At Common Law generally there was no clear prohibition imposed on the use of inside information except only in the case of industrial and trade secrets and details concerning customers.[21] In other respects, the director or other officer was free to hold and deal in the shares of the company.

STATUTORY INTERVENTION AND PROHIBITION OF INSIDER TRADING

In the recent Past, (and even now), because of the great danger which unrestricted use of inside knowledge can cause in dealings in company securities, various efforts were taken to check the abuse of such inside information.

Thus in the United States of America, an insider is obliged to disgorge his ill-gotten gains to the company or the person with whom he dealt.

In the United Kingdom, a more far-reaching step was taken by the company securities *(Insider Dealing) Act, 1985* which prohibits insider trading and prescribes penal sanction in the form of imprisonment for contravention.

In Nigeria, the control of "insider trading" was first contained in *sections 614-623 of the Companies and Allied Matters Act, 1990* which was repealed and replaced by section *81 to 98 of the Investment and Securities*

[21] British Industrial Plastics v. Ferguson (1938)4 ALL ER 504

Act, 1999, now sections 105 to 116 of the Investment and Securities Act 2007.

It should be born in mind that the provisions of the Nigerian statutes are based on the United Kingdom Act, with local amendments. Therefore, our comparative view of the

Provisions of the statutes may not necessarily involve a section analysis; rather a holistic or general explanatory approach would be adopted here.

WHO IS AN INSIDER AND WHAT IS INSIDE INFORMATION?

Any person who is or is connected with the company in one or more of the following capacities; that is, a director of the company or a related company; an officer[22] of the company or a related company; an employer of the company or a related company; an employee of the company involved in a professional or business relationship to the company, any shareholder of the company who owns 5 percent or more of any class of securities or any person who is or can be deemed to have any relationship with the company or member; and members of the audit committee of a company,[23] is an insider.

Where any of the persons listed above, and is (by virtue of having been) connected with any such person or connected with the company in any other way possesses unpublished price sensitive information in relation to the securities of the company makes a reference to information which: relates to specific matters relating or of concern (directly or indirectly) to start that company that is, is not of a general nature relating of concern to that company: and is not generally known to y to deal in those securities but which would; if it were generally known to them would likely materially affect the price of those securities, is what is referred to as *inside information".*[24]

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22 See section 567 of the Company and Allied Matters Act Cap C20 LFN 2007 which designates the following persons as officers of the company: directors, managers or secretaries.

23 See the Definition of Insider" (a)(i)-(vi) of section 315

24 Ibid 315 (b): see also section 56 (1) and 57 (1) of the Criminal Justice Act 1993.

In the same light, "*Insider Dealing"* has been described to include insider trading and occurs when a person or group of persons who being in possession of some confidential and price sensitive information not generally available to the public, utilizes such information to buy or sell securities for the benefit of himself, itself or any person.

The foregoing simply tells us that an insider is one who deals in securities and the Act further described the *Dealing in Securities"* to mean (whether as principal or agent) making or offering to make with any person, or inducing or attempting to induce any person to enter into or to offer to enter into: any agreement for or with a view to acquiring, disposing or subscribing for, or underwriting of security or any agreement the purpose or pretended purpose of securing a profit of any of the parties from the yield of securities or by reference to fluctuation in the price of securities.

By a community reading of the above provisions, one would be quick to note that:

a. A director, member, auditor (s) employer, or any person who is connected with the company or with any of the above named persons can be regarded as an insider.

   By a stretch of interpretation it can also be argued that servants of a company could be regarded as insiders if there is the established of professional or business relationship

b. Also, and d importantly, the inside information must be specific, precise and direct. The information must not be of a general nature, and the insider who deals in securities, must have induced, convinced or persuaded (or tried to do any of the following on) the other to deal in securities. Also worthy of note is the fact that such an information

   Must be confidential and price sensitive in nature and the insider must try to utilize such information to his benefit or to the disadvantage of another party.

An example of Insider dealing by a director can be found in *R v. Dickson*[25] where the defendant was the managing director of a subsidiary company

[25] Unreported but noted (1982) 3 Co Haw 1985

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who took out an option contract on shares in the Parent company ahead of an impending takeover.

In England, an individual who has information as an insider is prohibited from dealing in price affected securities,[26] encouraging another person to deal and disclosing the information, other than in the proper performance of the functions of the insider's employment, office or profession to another person.

CATEGORIES OF INSIDER DEALING

False Trading and Market Rigging Transaction

This occurs when a person deliberately creates or causes to be created, or does anything which may create a false or misleading appearance of active trading in any securities on a securities exchange or capital trade point or a false or misleading appearance with respect to the market or the price of any such securities.

Furthermore, an individual is not permitted to purchase or sell any securities that do not involve a change in the beneficial ownership of those securities or by any fictitious transactions or devices, maintain, inflate, depress or cause fluctuations in the market price of any securities. [27]

Securities Market Manipulation[28]

The investment and securities Act expressly prohibits any securities market manipulation which occurs where a person effects, takes part in, is

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[26] le Securities listed in Criminal Justice Act 1993 Schedule 2:S. 54(1) The dealing must take place on a regulated market or relying on or acting as a professional intermediary s. 52(1), (3).

[27] See Section 105 (1) & (2) ISA:
By subsection (3), any person who effects, or carries out either directly or indirectly any transaction, sale or purchase of any securities , being a transaction… which does not involve any change in the beneficial
Ownership of the securities… or a person who knows that associated with him has made or caused to be made an offer to purchase the same numbers of securities at a priced which is substantially the same or who makes or caused to be made an offer to sell the same number of securities at a price which is substantially the same as at the first mentioned price shall be deemed to have created a false or misleading appearance or active trading insecurities on a securities exchange or capital trade point.
N/B, a person can rely on the defence in subsection (4) that the he did intend to create a false market or false appearance.

[28] See Section 106 ISA

concerned in or carries out two or more transactions in securities of a body corporate being transactions which have or are likely to have effect of raising or lowering the price of the securities of the body corporate on a securities exchange or capital trade point with the intent to induce other persons to purchase, sell or subscribe for the securities of the body corporate or of a related body corporate[29]…

In our humble view, though the above provisions are generally described as "market abuse", it is also a form of "insider trading" which as we know, is defined by the position which an individual (Insider) occupies, as well as the information which he uses or manipulates to his advantage. Thus, in the above market situations, a person is expressly prohibited from creating a "false market appearance" which may have the effect of raising or lowering the price of the securities of a body corporate.

False or Misleading Statement,[30] Fraudulently Inducing Person to Deal in Securities

A person shall not knowingly, recklessly or negligently make a statement, or disseminate information, which is false or misleading in any material particular and likely to induce the sale or purchase of the securities by other persons or likely to have the effect of raising, lowering maintaining or establishing the market prices of securities.

Furthermore, by *section 108 ISA,* a person is expressly prohibited from making, publishing, promising or recording in any mechanical electronic manner, any misleading deceptive false or dishonest statement which

[29] Ibid Section 106(3) & (4) ISA. A reference to a transaction in relation to securities of a body corporate include a reference to the making of an offer to subscribe, sell or purchase such securities of the body corporate; and a reference to the making of an invitation however made which expressly or impliedly invites a person to offer to subscribe, sell or purchase securities of the body corporate.

By subsection (4), no securities of a public company listed on any recognized securities exchange shall bought or sold outside the facilities of a recognized exchange on which the securities are listed

[30] See Section 107 I.S.A

conceals material facts, or omit to state necessary material facts in respect of securities.

However, by *subsection (2)* of that section, it is a defence to any liability above, if it can be established that, at the time when the person so recorded or stored the information he had no reasonable grounds for expecting that the information would be available to any other person.

From the above provisions, it is observed that the law frowns upon the "fraudulent intent" as well as professional negligence or recklessness on the part of securities dealers' (insiders).

In the same vein, *section 110 I.S.A* frowns out rightly against the dissemination of illegal information which is to the effect that the price of any securities will or is likely to rise or fall or be maintained by reason of any transaction entered into or other act or thing done in relation to securities of that body corporate.

Also, no Person shall directly or in connection with the purchase or sale of any securities employ any device, scheme, artifice, or engage in any act, practice or course of business to defraud, or deceive any person.[31]

Prohibition of dealing in Securities by Insiders, and Abuse of Information obtained in Official Capital[32]

By the express provisions of *section 111(1),* except as provided in *section 104[33] of the Act,* a person who is an insider of a company shall not buy or

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31 See section 110 ISA.

32 Sections 111 and 112 of the ISA

33 Section 104 (1) & (2) ISA provides that for the purpose of preventing the excessive use of credit for the purchase or carrying of securities by dealers or member companies, the commission may make regulations to provide for margin requirements, for the amount of credit which may from time to time be extended and to maintained by securities dealers on all or specified securities or transactions or class of securities and transactions and for matters connected. (2) The commission may also make regulations for securities lending transaction by securities dealers.

N/B, "Securities lending" in section 315 means the temporary exchange of securities, generally for cash or other securities of at least equivalent values, with an obligation to redeliver a like quantity of the same securities on a future date and includes securities loans, repurchase agreement (Repos) and self-buy back agreements:

sell, or otherwise deal in the securities of the company which are offered to the public for sale or subscription if he has information which he knows is unpublished price sensitive information in relation to those securities.

(2) The above subsection (1) applies where: a person has information which he knowingly obtains (directly or indirectly) from another person who; is connected with a particular company, or was at any time within the six months preceding the obtaining of the information, so connected, the former person knows about, or has reasonable cause to know that the latter individual holds the information by virtue of being so connected; and the former person knows or has reasonable cause to believe that, by reason of the latter's connection and position, it would be reasonable to expect him not to disclose the information except for the proper performance of the functions attached to that position.

Note that the former person mentioned in subsection (2) shall not himself deal in securities of that company or any other company if he knows that the information is unpublished price sensitive information in relation to those securities and it relates to transaction (actual or contemplated) involving the first company and the other company, or involving one of them and securities of the other, or to the fact that any such transaction is no longer contemplated.

Furthermore, *section 112* deprecates the abuse of information which is held by a public officer; (whether by recent or former position) or is knowingly obtained by a person (directly or indirectly) from a public officer who he knows or has reasonable cause to believe held that information by virtue of any such position, and it is reasonable to expect a person in that position not to disclose such information except for the proper performance of the functions attaching to that position and the person holing it knows it is unpublished price sensitive information in relation to securities of a particular company.

By *section (3)* and subject to *section 113 of the Act,* a person whom section 112 (1) & (2) applies, shall not deal in any relevant securities; shall not counsel, procure or communicate to any other person the information held or obtained, if he knows or has reasonable cause to believe that he or some

other person shall make use of the information for dealing or of procuring any other person to deal on a securities exchange or capital trade point in any such securities.

INSIDER TRADING IN TAKE-OVER BID[34]

Where an individual is contemplating or has contemplated making a take-over offer for a company in a particular capacity, that individual cannot deal in securities of that company in another capacity if he knows that the offers is contemplated, or is no longer contemplated, and the offer is unpublished price sensitive information in relation to those securities. Also where a person has knowingly obtained from an individual in the above situation, information that the offer referred to in that regard is being contemplate or is no longer contemplated, the former person shall not himself deal in securities of that company if he knows that the information is unpublished price sensitive information in relation to those securities.

Noteworthy is the fact that a person who is for the time being prohibited by the provisions of section 111 from dealing on an approved securities exchange or capital trade point in any securities shall not counsel or procure any other person to deal in those securities, knowing or having reasonable cause to believe that the person would deal in those securities.

Actions not prohibited by section 111 and 112 as dealing in securities by insiders.

Section 113 provides that an individual is not by reason of his having any information prohibited from any of the following actions-

i. Doing any particular thing otherwise than with a view to the making of a profit or the avoidance of a loss by the use of that information.
ii. Entering into a transaction in the course of the exercise in good faith of his functions as liquidator, receiver or trustee in bankruptcy.
iii. Doing any particular thing if the information.

[34] See Section 111 (4) and (5) and (6)

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- Was obtained by him in the course of business of a stockbroker; and
- Was of a description which it would be reasonable to expect him to obtain in the ordinary course of that business and he does that thing in good faith in the course of that business; and
- Doing anything as above in relation to any particular securities.

CIVIL REMEDIES UNDER THE INVESTMENTS AND SECURITIES ACT

Voidable Transactions[35]. Any transaction done in contravention of section 111 or 112 of the Act is voidable at the instance of the commission.

Compensation[36]

A person who is liable under part XI of the Act shall pay compensation at the order of the commission or the Tribunal, as the case may be. The compensation is payable to any aggrieved person who in a transaction for the purchase or sale of securities entered into with the mentioned person or with a person acting for or on his behalf, suffers a loss by reason of the difference between the price at which the securities would have likely been dealt in such a transaction at the time when the first mentioned transaction took place, if the contravention had not occurred. The amount of compensation payable is the amount of the loss sustained by the claiming the compensation or any other amount determined by the commission or the tribunal.

Establishment of investors protection fund

Section 197 of the Act provides that a securities exchange or capital trade point shall establish and maintain a fund to be known as the investors' protection fund which shall be administered by a board of trustees on its behalf.

The objective of the fund is to compensate investors who suffer pecuniary loss arising from the insolvency, bankruptcy or negligence of a committed

[35] Section 114 I.S.A.
[36] Section 116 (1) & (2) I.S.A.

by a dealing member firm or any of the directors, officers employees or representatives in relation to securities, money or any property entrusted to, or received by the dealing member firm in the course of its business as a capital market operation.[37]

From a comparative perspective, we observed that insider dealing has been controlled for some time in USA, on the basis that an insider in a fiduciary position must not profit from information obtained by virtue of that position, unless permitted by the person to whom the fiduciary duty is owed.[38]

In England or UK, the insider dealing is provided for in the Financial Securities and Market Act (FSAMA) 2000, part VIII, the Criminal Justice Act 1993 and the Companies Securities (Insider Dealing) Act 1985. The Nigerian provisions are impari material with the above statutes in terms of insider regulations[39] and penalties.

Here, apart from those members and officers of the company, journalists could also be regarded as insiders.[40]

Hence, by the *Press Complaints Commission Code of Practice* (financial, journalism) states:

i. Even where the law does not prohibit it, journalists must not use for their own profit financial information they receive in advance of its general publication, nor should they pass such information to others.
ii. They must not write about shares or securities in whose performance they know that they or their close families have a

[37] Section 198: it should also be noted that the funds consists of all monies paid to the Board of Trustees by the dealing members of the securities exchange and capital trade point, interest and profits accruing from the fund, money recovered by the board and other monies lawfully paid into the fund.

[38] United State v. O' Hagan (1997)251 US 642

[39] See section 118 (B) 118 (C) of FSAMA 2000

[40] Devek French and Stephen Mayson. *Company Law 2010-201 edition*, (London, Oxford University Press

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significant financial interest without disclosing the interest to the editor or financial editor.

iii. They must not buy or sell, either directly or through nominees or agents, shares or securities about which they have written recently or about which they intend to write in the near future.

ADDITIONAL CIVIL REMEDIES THROUGH THE FSAMA 2000

Under the Act, *section 123 (1) (a)*

Financial Penalty or Censure: If the FSA is satisfied that a person is, or has, engaged in market abuse, it may impose a financial penalty or publish a statement to that effect that the person has engaged in market abuse[41].

The same sanctions are available if the FSA is satisfied that a person, 'A', has required or encouraged another or others to do something which would amount to market abuse if done by 'A'. Moreso, the imposition of a penalty does not make any transaction void or unenforceable. (*s. 131)*

The Act empowers the High Court under section (381(5)) on the application of the FSA, to issue an injunction restraining apprehended or continuing market abuse. The court may order a person to take steps to remedy or mitigate market abuse in which the person has engage and if the court is satisfied that a person may be, or may have been, engaged in market abuse, it has power to issue a freezing injunction restraining the person from disposing of, or dealing with assets[42].

The FSA may make a restitution order against a person who has engaged in market abuse, or who has required or encouraged another to do so, or may apply to the High Court for it to make an order. A restitution order may be made against a person only if either that person has profited as a resulted of the abuse or one or more other persons have suffered loss or been otherwise adversely affected as a result. The money which is paid under a restitution order goes to the person or person to whom the profits are attributable or who have suffered the loss or adverse effect, and the amount is determined having regard to the size of the profit or loss.

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41 (*s. 123(3))*

42 (section 381(3) & (4))

RECOMMENDATION

While we appreciate the extent of the development of our laws with respect to insider dealings, we boldly make the following recommendations:

1. The position in England should be adopted whereby certain class of persons (such as journalists) who are not necessarily part of company may be regarded as insiders because of the sensitive position which they occupy in the society.
2. We also recommend that section 144 of the Investment and securities Act be amended to the effect that, any transaction done in contravention of section 111 and 112 of the Act is voidable at the instance of the court and not necessarily the commission which may connive with an insider to validate such transactions.
3. We also suggest that the ISA be amended to include more civil remedies available to the individual. Remedies such as: action for the damages for breach of contract, specific performance, injunctions, restitutions and prohibitions.

CONCLUSION

In view of the provisions of the relevant laws on insider trading, it is apt to say that, the law is aimed at nipping in the bud, the use of price sensitive information to the undue advantages of persons who occupy certain key positions in the securities market or body corporate, and at the same time making provisions to remedy any loss incurred by an individual.

We noticed very evidently that the investments and securities Act, as well as the criminal justice Act above criminalize insider trading. In the same vein we have considered the civil remedies available to an individual who fall victim of "insider trade".

Consequently, one pertinent question which demands attention is whether the general common law and equitable remedies are potent and effective deterrents.

Although a great advantage of the civil suit brought by the company for breach of fiduciary duty or breach of confidence is that it does not have to

show that it has suffered loss as a result of the insider dealing rather that the made an undisclosed profit. [43]

The point here is, what about persons who are insiders but do not owe any fiduciary duties to the company?

The above explains the reason for or the criminal penal sanction adopted by the regulatory statutes, (please note that the criminal sanctions are outside the purview of this work) and other remedies considered above. *(Compensation, Discretion to void the agreement, injunctions and restitutions)* thus, where an individual is not criminally liable depending on the level of the breach or involvement as an insider.

[43] The leading case is the decision of the New York Court of Appeals in *Diamond v. Oreamuno* (1969) 248 N.E. 2d 190

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