**CRITICAL APPRAISAL OF THE CONCEPT OF INSIDER TRADING UNDER NIGERIAN COMPANY LAW**

ABSTRACT

Insider trading has been understood to the act of dealing in unpublished price sensitive information and it is seen to go against the principle of equal access to information. This work made an unfair appraisal of the concept of insider trading in Nigeria in the course of the work. The origin of inside trading regulation was examined and a cursory literature review of the concept of insider trading was made. In the courses of examine the overview of this concept, the argument both for and against the prohibition of insider trading was made. This study paid primary attention to the prohibition of regulation of this concept in Nigeria from its conception to date. A look was taken at the regulation of the concept in some other jurisdiction and finally some recommendations were made.

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**CHAPTER ONE**

**1.0 INTRODUCTION**

As the business world continues to expand in global markets, trading of shares, bonds, derivatives and other instruments continue to increase. One corm of trading that has received considerable interest in recent years is insider trading.[[2]](#footnote-1) Insider trading occurs when individuals with potential access to non-public information about a corporation buy or sell stock of that corporation. When the information is material and non-public, such trading is illegal. In these cases, individuals are aware non-public information gained through the performance of their duties and thereby are in breach of a fiduciary or other position of trust.[[3]](#footnote-2) However, if the trading is done in a manner that does not take advantage of non-public information, it is often permissible. For example, if a director of a company knows that the company is crashing due to some unsuccessful business risks, and then sells his shares knowing that the board has decided to cut the dividend and that this will be announced in a few days, he is guilty of insider trading.[[4]](#footnote-3) In a similar vein, where a director knowing that diamond or has been discovered on the company’s land, without the fat being known to the public, buys more shares in anticipation of a considerably high rise in the value of shares, he is also guilty of insider trading. It is clear that the use of such “insider” information by an insider to benefit himself at the expense of others, not so well places, is unfair.[[5]](#footnote-4) The director, as we have seen earlier, owes a fiduciary duty to the company, and so if he is allowed to use his inside knowledge of the affairs of his company for his personal benefit then a conflict of interest is inevitable. This is apart from the unfairness to the individual shareholders.

Regulation and enforcement of insider trading laws is important to investors for a number of reasons.[[6]](#footnote-5) The first reason is that investors are likely to be more confident in the financial statements of companies that operate in countries with strong insider trading laws if such laws are enforced consistently. In addition, investments within such countries may be viewed as less risky as the informant is considered to be more reliable. Finally, as risk and the return investors require on an investment are positively correlated investments may have a lower required rate of return.[[7]](#footnote-6)

**1.1 BACKGROUND**

Insider trading is one of the corporate ills that have existed since the emergence of the abstract entity known as company.[[8]](#footnote-7) Incidentally, this corporate evil has existed unchecked for over a century of the development of company law. As noted by Orojo[[9]](#footnote-8), at common law no clear prohibition was imposed on the use of insider information except only in the case of industrial and trade secrets.[[10]](#footnote-9) In other respects, the directors or other officers were free to hold and deal in the shares of the companies.[[11]](#footnote-10) The lack of legislative check on the ills of insider trading was feature of company law in most jurisdictions including Nigeria until recently.[[12]](#footnote-11)

In the United Kingdom it was not until the mid-80, whens Ivan Boesky, an American admitted to large scale dealings on the basis of insider information, and handed over some 100 million USW Dollars of alleged profit to the security and Exchange Commission and other instances of the practice involving ring of bankers, lawyers and others that issues of insider trading came to the Iront burner of company legislation in England, ultimately resulting in the passing of the **Company Securities (Insider Dealing) Act 1985.**

The United States of America has historically been the world leader in insider trading law. In 1909, the US. Supreme Court ruled in **Strong v Repids[[13]](#footnote-12)** that because a company director could affect the value of his company’s shares, keeping buyers ignorant of his expected actions while selling his own shares would be deceitful and therefore fraudulent. This case was the first major step in the foundation for insider trading in which an insider was obliged to disgorge his ill-gotten gains to the company or to the persons with whom he dealt.[[14]](#footnote-13)

Insider trading was not treated as a statutory offence in Nigeria until 1990. The move towards a prohibition and the regulation of insider trading in Nigeria was orchestrated by the Nigerian Law Reform Commission. The acknowledge that insider trading was a serious malpractice.[[15]](#footnote-14) The recommendation of eh commission led to the enactment of provisions on insider trading prohibition in **Section 614 – 620 cof the companies and Allied Matters Act 1990.[[16]](#footnote-15)** The provisions were copied from the **English Company Securities (Insider Dealing) Act 1985.** However, the above provisions of **CAMA** turned out to be inadequate and ineffective for purpose of combating insider trading, because for almost ten years after its inception, no person was successfully prosecuted under the sections. Consequently, the provisions under **CAMA** were repealed and replaced by the **Investment and securities Act 1999**. **The 1999 Act** has been repealed and replaced by the **Investment and Securities Act 2007.[[17]](#footnote-16)** The new provisions like its predecessors have its own flaws as not person is also yet to be reported to have been convicted of insider trading.

**1.2 STATEMENT OF THE PROBLEM**

One of the major challenges which various jurisdictions across the globe is facing in respect of companies is the control of insider trading. There are some countries that are at eh forefronts in the fight against insider trading and they include the United States of America, the Greek, British, etc.

Insider trading being a global issue is also being tackled in Nigeria. Nigeria woke up to the fact that insider trading is a serious malpractice in 1988 following the report of the Nigerian Law Reform Commission. In accordance with the recommendation of the commission several laws have been made to control this corporate. Regrettably, unlike what the position is in the United State, British and some other jurisdictions, no successful conviction has been recorded for insider trading in Nigeria in spite of the metamorphosis we have had in the laws regulating insider trading in Nigeria that has made it difficult for the law to successfully catch at least one person.

**1.3 RESEARCH QUESTION**

Against the background of the research objectives, the following are the research question for investigation.

1. What is insider trading?
2. What is an insider?
3. Who is a connected person?
4. What is unpublished price sensitive information?
5. To what extent has the Investment and Securities Act 2007 assisted in the light against trading in Nigeria?
6. Is there the need for amendment?

**1.4 AIMS AND OBJECTIVES OF THE STUDY**

The broad aim of this work is to do a critical appraisal of the concept of insider trading under Nigerian company law. To this end, the specific objectives of the work include:

1. To give a general overviews of the concept of insider trading
2. To assess the effect of insider trading on the development of Nigeria.
3. To analyze the approaches to insider trading
4. To appraise the role of the Security and Exchange Commission in the Securities Act relating to insider trading have succeeded or failed in its quest to control insider trading in Nigeria.

**1.5 RESEARCH METHOD**

In the course of doing a critical appraisal of the concept of insider trading under Nigerian company law, the researcher adopted hermeneutical of the various materials studied.

**1.6 SIGNIFICANT OF THE STUDY**

The important of this work stems from the huge benefit it will bring to everyone that may develop an interest in the elimination of insider trading in Nigeria. A remarkable and interesting contribution of the study is the boost that the findings from the investigation will give to everyone interested in the fight against the menace called insider trading.

In addition to the aforementioned significance of the study is the fact that it will add to the studies previously carried out in respect of insider trading which will at the same time reinforce the prevailing opinion among scholars.

**1.7 LIMITATION AND SCOPE OF THE STUDY**

To complete this work without an expression of the imitation encountered may amount to an unhealthy presumption. To this end, the work set out to critically appraise the concept of insider trading under Nigerian company law. Though this work may appear to be comprehensive, it cannot be said to be an exclusive appraised of the concept of insider trading under Nigeria company law.

Another limitation encountered in the course of this study is scarcity of local material dealing on insider trading despite the fact that insider trading is not a new concept. There is also a limitation in respect of time. Since this study has to be concluded within a few months, the line needed to thoroughly investigate is short.

**1.8 DEFINITION OF TERMS**

**1.8.1 INSIDER**

The black’s law dictionary[[18]](#footnote-17) simply defined insider thus:

1. A person who has knowledge of fails not available to the general public; 2. One who takes part in the controls of a corporation, such as an officer or director is one who owns 10% of more of the corporation stock .

The term insider is, however, comprehensively defined under Section 315 of the investment and securities Act thus

“Insider” means:

1. Any person who is connected with the company in one or more of the following capacities
   1. A director of the company or a related company;
   2. An officer of the company or a related company;
   3. An employer of the company or a related company;
   4. An employee of the company involved in a professional or business relationship to the company.
   5. Any shareholder of the company who owes 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;
   6. Member of audit committee of a company; and
2. Any of the person listed in paragraph (a), who by virtue of having been connected with any other way, possesses unpublished price sensitive information in relation to the securities of the company is reference to information which:
   1. Relates to specific matters relating or of concern (directly or indirectly) to that company that is, is not of a general nature relating or of concern to that company; and
   2. Is not generally known to those who are accustomed to or would be likely to deal in those securities but which would, if were generally known to them be likely material to affect the price of those securities.

**1.8.2 TRADING**

The Black’s Law Dictionary[[19]](#footnote-18) simply defined the term “trading’ thus

The business of buying and selling, especially, of commodities and securities.

**1.8.3 INSIDER TRADING**

It has been explained that insider trading occurs where an individual or organization buys or sells securities while knowingly in possession if some piece of confidential 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.

Under the Investment and securities Act 2007 insider trading was termed “insider dealing” and defined thus

Insider dealing includes insider trading and occurs when a 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 Black’s Law Dictionary define trading as the use of material, nonpublic information in trading the share of a company by corporate insider or other person who owes fiduciary duty to the company. This is the classic definition. The Supreme Court has also approved a broader definition known as the “misappropriation theory” the deceitful acquisition and misuse of information that properly belongs to persons to whom one owes a duty.

**1.8.4 SECURITIES**

The Black’s Law Dictionary[[20]](#footnote-19) defines security as collateral given or pledged to guarantee the fulfillment of an obligation; especially the assurance that a creditor will be repaid (usually with interest) any money or credit entered to a debtor. An instrument that evidences the holder’s ownership rights in a firm (e.g a stock), the holder’s creditor relationship with a firm or government (e.g; a bond), or the holder’s other rights (e.g. an option)

Under the Act the term securities was elaborately defined thus

Securities means

1. Debentures, stocks or bonds issued or proposed to be issued by a government;
2. Debentures, stocks, share, bonds or notes issued or proposed to be issued by a body corporate;
3. Any right or option in respect of any such debentures, stocks, shares, bonds or notes; or
4. Commodities futures, contracts, options and other derivatives and the term securities in this Act includes those securities in the category of securities listed in (a) – (d0 above which may be transferred by means of any electronic modes approved by the commission and which may be deposited, kept or stored with any licensed depository or custodian company as provided under this Act.

**1.8.5 TIPPEE**

According to the Black’s Law Dictionary a tippee is a person who acquires material nonpublic information from someone in a fiduciary relationship with the company to which the information pertains[[21]](#footnote-20).

**1.8.6 TIPPER**

The Black’s Law Dictionary defines a tipper as a person who is a fiduciary relationship with a company that the person possess material inside information about, and who selectively discloses that information for trading or other personal purposes[[22]](#footnote-21).

**1.9 LITERATURE REVIEW**

Insider trading literature review will focus on issues with its regulation from the view point of law and economics. Law and economic literature categorize insider trading studies into two categories – the agency theory and the market theory of insider trading[[23]](#footnote-22). The agency theory of insider trading deals with the impact of insider trading on firm-level efficiency and corporate value (Jensen and Mecking, 1976). On the other hand, the market theory of insider trading analyzes the implication of insider trading on market performance, (Bhattacharya and Daouk (2000) for instance, the cost of capital, this liquidity and the market efficiency etc. For example, Manna (1966) suggests that insider trading allows stock markets to be more efficient. Surprisingly, most of the debates on insider trading are concentrated on the U.S stock markets. Whereas, La Posta et al claim that laws and their level of enforcement vary according to countries infrastructures. Moreover, differences in laws and their enforcement may explain variations in market structures and stock market practices among different countries. Maug present a mathematical model in which a dominant owner has information advantage over small shareholders where insider trading regulations are properly enclosed. Besides, Leland argues that if insider trading is allowed, stock prices reflect information at the cost of loss liquidity and the magnitude of liquidity decreased varies with the economic environment of a country.

Baiman and Verrocchio (1996) argue that the level of insider trading varies with level of financial disclosures, the culture, and the economics of difficult countries. Therefore, it can be expected that the impact of insider trading archives on the on the stock market varies country to country. Bhattacharya and Daouk (2002) address the effect of insider trading regulation and its enforcement on the cost of capital in 51 countries over more than 20 yours. They hind that insiders trading regulation and its enforcement help in reducing the cost of capital of the firm. However, the magnitude of effect varies with the level of enforcement of a country. Moreover, Beny (2005) does attempt to find whether insider trading law matters his the ownership dispersion, the stock price informativeness and the stock liquidity. In empirical results, he finds that ownership dispersion, stock price informativeness and stock liquidity are greater where insider trading law and its enforcement are strict. Moreover, most important aspects of the formal law are penalties and criminal sanctions that are imposed on who violate insider trading law.

Fernandez and Ferreira (2009) argue that insider trading regulation and its enforcement improve the informativeness of stock prices, but this improvement is concentrated in developed markets. For these results, they suggest that borrowing insider trading regulation from a developed market may not be effective if an emerging market’s infrastructure is not complementary to a developed markets infrastructure. In addition, Kerner and Kucik (2010) argue that not only a country’s specific factors influence the tightness if insider trading regulation and its enforcement but also the investment factors of international competitiveness, explained by pressures to attract more foreign investors. Because in order to attract more foreign investors, a country has to establish an investor-friendly regulations and its enforcement. Recently, Chauhan et al. (2012) examine the effectiveness of insider trading regulation while the production of private information via insider trading. They also interact this natural experiment with product market imperfection. For this they argue that in the absence of effective coordination between product market and stock market to frame regulation, the outcome of regulation intervention will not be homogeneous among heterogeneous firms. In the empirical findings, they find that regulation interventions improve the information content of insider trading. However, the magnitude if improvement varies along with the category of insiders, the position of a firm in product market competition, firm officers’ trades and insider trades in lows product market firms produce higher information content compared to other group of firms.

Ebrahim and Black (2013) investigate the impact of corporate governance mechanisms, particularly board independence, on profitability of insider trades before and after the 2002 enactment of Sarbanes- Olney (SOX). They show that corporate governance mechanisms can be used to reduce the shortcomings of existing regulations or their enforcement mechanisms in reducing the incidents of information-driven trades.

**CHAPTER TWO**

**AN OVERVIEW OF INSIDER TRADING**

**2.0 INTRODUCTION**

The purpose of this chapter is to discuss extensively the theory concerning the problem of insider trading as well as the arguments in support and against its regulation.

Obviously, it is not generally agreed that insider trading should be prohibited. In a similar vein, it is also not generally agreed that insider trading is wrong. This position is the same even in jurisdictions where insider trading is being regulated; some of the people of such jurisdictions still believe that it should not be a harm to make money by getting inside information of a corporation.[[24]](#footnote-23) It is however, noteworthy that it has been said that insider trading is the unacceptable face of capitalism. But some others do not see anything wrong with insider trading and even think it should be encouraged.[[25]](#footnote-24) This is a view which economists and lawyers have put forward ever since professor Manne[[26]](#footnote-25) published his book in 1966 titled Insider Trading and the Stock Market. This book emphasized that insider trading is, in the economic sense, positively beneficial and ought not to be prohibited. Since then the debate on regulation has raged between those who would support Prof. Manne’s position and consider the problem in terms of economic efficiency alone and those whose arguments for prohibition would be based on market integrity, notions of fairness and morality. The arguments for and against insider trading prohibition as well as the legal and moral reasons for its prohibition will be considered hereunder.

**2.1 FAIRNESS AND EQUALITY OF INFORMATION**

It is understood that one of the reasons why the debate over whether insider trading should be regulated came about due to the ‘fairness’ concept to justify regulation in the U.S by the Securities and Exchange Commission (SEC) and the courts. In Re Cady Roberts & Co[[27]](#footnote-26) the SEC based its decision to prohibit insider dealing on grounds of ‘fairness’ and it was the same outcome in SEC v. Texas Gulf Sulphur Co.[[28]](#footnote-27) The court’s finding was;

…”to prevent in equitable and unfair practices and to inside fairness in securities transactions generally, whether conducted face-to-face, over the counter, or on exchanges… the Rule [meaning Rule 10b-5] is based in policy on the justifiable expectation of the securities market place that all investors trading on impersonal exchanges have relatively equal access to material information”.

Professor Manne, one of the defendants of insider trading argue that insider dealing should not be regulated at all and he criticized the legal grounds for regulating insider trading. He argues that there has been no careful analysis of the subject. He believes that in the absence of sufficient economic analysis, the attitude of the debate turns to moralistic and emotional issues instead of logic.

Moore[[29]](#footnote-28) does not support the theory of fairness. She explains that one is not morally obligated to tell those whom we deal with everything that is in their interest to know. However, there is the idea that there should be absolute equality between market participants. Due to the observation that insider trading is largely based on the idea that it is unfair. In order to maintain fair transactions, it would only be reasonable that investors in the market have equal access to information, it is considered to offend the notion of fairness. ‘Fairness’ as a concept has therefore been resorted to as a justification for regulating insider trading.

The legal philosophy of fairness considers it unfair when insiders have an advantage and a better bargaining position than outsiders, based on this, probably the most practicable justification for the regulation of insider trading is equality of information. Information as to the basis of decisions made by investors should be equally available to all investors. Thus, all traders owe a duty to the market either to disclose or obtain from trading based on non-public information. This approach is compatible with the need to make public as much information as possible so investors will be equally informed.

Equality of information (market egalitarianism) requires that all investors trading on impersonal exchanges should have relatively equal access to material information. However, regulating insider trading has attracted its share of criticism. Professor Manne tried to argue against the ethics of insider trading by stating that he thinks fairness as an argument for regulating insider trading is a respected concept, but is difficult to determine. He thinks relying on fairness is vague and cannot be defined, let alone be used as an argument for regulation. However, those who argue fairness as a justification for regulation reject these conditions. Their belief is that Prof Manne ignores the fact that ‘fairness’ is the dominant premise underlying our understanding of the law. In challenging the ground of fairness, Manne depended on two grounds. His first ground being that the inequality in bargaining positions between the parties in a share transaction and between investors in the market is an inevitable fact. He believes that no law or regulation can ensure equality of bargaining position and he also believes that there is always inequality in terms of information between the parties in share transaction. The stock market, according to him, is an information exchange. The second ground for criticism is that he believes that insider trading is a victimless crime. He believes that in anonymous market dealing, the insider deals with a person as a result of the random matching of orders and this person would have deal anyway of the same market price at the same moment in time. So in his view, this goes to show that the other party to insider trading is not misled or harmed by the insider and there is no unfairness to him. However, it should be noted that although it is not possible to show the causal link between the activities of the insider and the outsider’s dealings which then incurs a loss, it may still be possible to regard the outsider as a victim of an informational advantage possessed by the other people in the market of which he is ignorant, and which he could not have obtained. Although it is accepted that it is not possible to put people on a completely equal loofing, for there will always be transactional inequalities and informational advantages based on superiors experience, foresight and diligence. It is argued that it should be possible to remove informational advantages achieved unfairly through access to information which cannot be obtained by others and which in all probability is being used by the insider in breach of some fiduciary or other duty.

All things considered, Manne’s hypotheses seem weak and simplistic. One significant response to Manne’s arguments is that the ‘fairness’ principle should not be narrowly interpreted as equivalent to the protection of investors. If it is expected that insider dealing will be harmful, not necessarily to a particular investor but rather to the market as a whole, for reasons of public policy, such acts should be regulated.

**2.2 INSIDER TRADING AS A MEANS OF COMPENSATION**

Manne maintains that his main argument is that allowing insider trading is the only effective means of compensating entrepreneurs. He argued against the notion that insider trading harm investors. He distinguished between corporate managers and entrepreneurs. He stated that managers do not include innovators. He believes that their work is a mere service which includes operating the firm normally and that such work is predictable therefore a salary can be sufficient compensation. On the other hand, he believes that entrepreneurs provide innovative contributions to the productivity of the firm. Manne argues that allowing insider trading is the only appropriate means of compensating entrepreneurs so that they will be given an incentive to produce more information. He stated that a predetermined salary not reflect the services provided by the entrepreneur, since it does not reflect the value of the innovation. He argues that only allowing entrepreneur to buy securities prior to a public disclosure, and to sell them after the price rises following the disclosure, is the appropriate method to value his innovation.

Carton and Fischel[[30]](#footnote-29) maintain this view. They argue that advanced salary agreements fail to compensate innovators. They believe that allowing insider trading enables agents to receive their compensation. Insider trading provides more accurate valuing of agents’ innovations than a salary. It is therefore argued that more incentives should be given to agents in other that they produce information.

These proponents of insider trading argue that by permitting insider trading, the interests of the insider will be aligned into that of the company. They believe that at the end of the day, the shareholders benefit from the acts of the insider and this is because the corporate insider may find it beneficial to enhance corporate risk taking thereby, developing growth and opportunities that will increase the value of shares of the company to which the shareholders will benefit from. However, this idea has been criticized as being flawed because a person who benefits from trading on insider information is not necessarily the innovator. Insider trading enables the insider profit whether their ideas fail or are successful in that they profit from both negative and positive information whereas the company may not. Even if the negative or false information did not pose problems for the company, the argument for insider trading as an incentive overlooks the difficulties posed by “free rider” those who do not actually contribute to the creation of the information, but who nevertheless are aware of it and can profit by trading on it. Unless those who not contribute can be excluded from trading on it, there will be no incentive to produce the desired information. Besides to create added value to the company will entail a significant investment of time and energy on the part of the insides to generate new information in order to profit from inside trading. It is often said that it would be equally profitable and much easier for the insider to start a rumour that the company is about to strike a deal or has acquired a new product rather than actually invent a new product.

It appears that in considering insider trading for innovation, Manne has failed to acknowledge the properly right of the firm to such information. For it is establishment that a company has a property right to the information produced inside the company, or if the case is that the insider is entrusted not to use such information, then obviously it is wrong to propose that the use of such information should be allowed as the most appropriate means of compensation.

It has been said that insider trading is not necessarily a better compensation than a salary. It is believed that a company is best placed to assess whether or not an employee is expected to provide innovative ideas. Rider and Frrench[[31]](#footnote-30) state that Manne does not explain why insiders should be permitted to benefit from producing negative news. Because allowing insiders to deal on the basis of negative news. Because allowing insiders to deal on the basis of negative inside information allows them to evade losses whether the company succeeds or not and they are supposed to be acting in the best interest of the company. If a manager was behind a loss to the company, why should he be able to avoid personal loss by allowing him to sell his own shares before the information is made public? Anything done on behalf of the company must be in the best interest of the company and insider trading hurts the company (its reputation its standing in the capital market). So it is not in the best interest of the company and should therefore be prohibited.

**2.3 OPTIMAL OR TIMELY DISCLOSURE**

Companies generate a lot of information as they catty on their business activities and that is why information plays a vital rate in an economy. The extent to which information is made available on the market influences the degree of economic efficiency. Stephen Bainbridge[[32]](#footnote-31) believes that to have a successful regulation of insider trading requires rules relating to the timely disclosure of material information. He believes that if the aim is to put investors on an equal footing in regards to having access to inside information, the rules governing insider trading are not the proper method to achieve it. And therefore disclosure requirements could be designed to keep minimum non-public price sensitive information in a way that the opportunities for abusing such information would be reduced. His belief is that disclosure requirements are a better solution than regulating insider trading in order to achieve informativeness in the market. This statement leads to questioning the competence of regulating insider trading, and supports the case that the problem is better dealt with by continuous disclosure. His belief is that effective regulation of insider trading on such a ground would not lead to an advanced disclosure system. This argument was establishment in the U.S, where the law had been reluctant to compel issuers to disclose material non-public information. It was therefore declared that, irrespective of permitting insider trading or not, the investors will not have the same access to information as insiders unless there is a system of timely disclosure. However the revelations from Enron to world can have further exposed the inadequate material disclosure of information, not only in the United States, but also in Nigeria.

The information product is a commodity and is only gathered when it is cost effective to do so. The idea is: the more information available, the greater the economic efficiency. Companies produce information to profit from it and it is argued that where insider trading is permitted, insiders will be motivated to get more information in order to profit from proponents of insider trading believe that when insiders trade in securities on the secondary market, they speed up the flow of information and feed their knowledge into prices, thereby making market more efficient. Therefore if insider trading is permitted and insiders with fore knowledge trade in securities of their company, it will be a signal to outsiders observing the price movements to infer that the insiders are optimistic about the company’s future prospects and may in turn buy shares which may cause the price more in a certain direction. It is, however, asserted that even when insider trading is informative and could be a channel of communicating information, it would often be preferable if insider information were communicated directly to the public rather than through the stock market. This will be better than an unexplained rise in the price of the firm through the trading activities of insiders.

There is however, a challenging view that insiders withhold and manipulate information in order to cash in thereby distorting market efficiency. Indeed, insider trading might be expected to induce a variety of perverse behaviours by managers who would compete to acquire and hoard information within the firm. The notion that disclosure rules are the primary method of reaching market informativeness is reasonable but it should be understood that regulation of insiders trading has a preventive roles in circumstances where an unexpected event occurs, the issuers will need more time to clarify the situation otherwise, an immediate announcement might cause false or misleading disclosure. In certain situation, the issues is exempted from making a lively disclosure, if it is thought that such disclosure would be determined to the legitimate interests of the issuer. In such situation the information should be kept confidential. It is these circumstances which are crucial for insider dealers, and therefore the regulation of insider trading is essential to prevent misuse of information during this period. Thus, disclosure rules alone are not sufficient enough to achieve informativeness in the market and so regulation of insider trading is essential.

**2.4 MARKET EFFICIENCY**

One other argument Prof. Manne postulates is that insider trading creates market efficiency. He argues that insider trading acts as a replacement for the public disclosure of inside non-public information. He argues that when insiders deal on the basis of inside information, they gradually bring the market price to a more realistic informed level. This is what Gilson and Kraakman call a ‘derivatively informed trading mechanism’. The suggestion is that uniformed investors will be informed through market information, meaning that through volume, number and trend of trades. He argues that a gradual adjustment is better than violent price fluctuation. His belief is that insider dealing is an effective way to release information into the market.

Gilson and Kraakman however, pointed out that derivatively informed trading function slowly and sporadically. So it is unlikely that allowing insider trading will have much effect on market efficiency. However said, insider trading may be a factor for nudging prices in a particular direction as the up to date position of the company becomes known to the market but in many cases, the disclosure of that information would have occurred regardless of any related insider trading.

The hypotheses of insider trading influence on the market price is uncertain. There are circumstances where insider trading is influential, e.g. the period prior to an announcement of takeover offer. One of the most interesting fails to emerge from Boesky investigation in the United States is the link which was exposed between insider trading and take-over bids. It is however doubtful whether the influence by insider is the usual trend is just an exception.

Assuming, for the sake of argument, that insider trading moves prices in the right direction, in the long term it is expected that uninformed investors inability to acquire information would be detrimental to the market. Those who argue in favour of deregulation base their argument on the idea that it is form of disseminating information into the market. Nevertheless, it has not been proven that indirect disclosure of information into the market is more efficient than direct disclosure.

Insider trading has an effect on the transaction costs market participants bear. The superior information insiders possess generates informational argumentry on capital markets. Asymmetry information increases the cost of trading. Insider trading on non-public information might reduce market liquidity. Reduced market liquidity implies higher trading costs. In order to achieve maximum efficiency, the most prompt disclosure possible of material information is therefore necessity. The more efficiently information about a security is reflected in price, the more efficient the market for that security is thought to be. It is not clear the point to which information quickly becomes public with or without insider trading. However, what is clear is that market prices are more accurate once the information is released. Investors believe that they will earn fair returns on this investments so permitting insider trading would create opportunity for exploitation of the market by insiders at the shareholders or investors expense. If investors believe that insider trading exists, they may reduce their investment in the securities of that company and this reduced investment will have unsetting effect on the overall liquidity of financial markets and the ability of companies to raise capital. Therefore, this will affect the allocation of resources and hence the attainment of market efficiency.

**2.5 PROTECTION OF INVESTOR CONFIDENCE**

Another ground for regulating insider trading would be to maintain market confidence. This is vital for the efficiency of the market. If investors perceive that the market is unfairly favouring insiders, they will not direct their investment into the market. It is therefore imperative that investors confidence be protected and that serves as a sufficient justification for regulating insider trading. Rider and Ashe indicate that the main convincing justification for controlling insider trading is that it has a perceived adverse impact on confidence. For the financial markets to be effectively operated, confidence and integrity is essential. Investors will only invest into a market they believe to be reasonably managed and regulated. If the public perceptions of the capital market is negative, investors will detect liquidity to alternatives and companies will therefore lose customers. Capital markets play a major role in allocating resources and confidence in them. Therefore there is the need to maintain confidence and integrity of capital markets. However, investors confidence as a rationale was criticized as an emotional and sentimental force which is thought to be speculative. Therefore, justifications based on protecting investors’ confidence are said to be unsophisticated, and the relationship between insider trading prohibition and investor confidence is a myth. Investors consider it their right to have equal access to information so their lack of confidence is only logical if insiders are allowed to be advantaged over other investors. Therefore, investor confidence is not necessarily an emotional force. It is rather based on the expectation of investors equally in terms of access to information.

**2.6 FIDUCIARY RELATIONSHIP**

The other reason put forth for the regulation of insider trading is the concept of fiduciary relationship which could be attained to the insider. It is clear that the directors of a company owe a fiduciary relationship with shareholders individually. This is also the case of common law.

According to the notion of breach of fiduciary relationships, insider trading regulation is derived from identifying that a price legal relationship has been breached. The idea here is that corporate insiders owe a disclosure duty based on a pre-existing relationship with the company. Insider trading here is justified on the basis that the insider is in a position of trust and so should be legally responsible to return any profit he has made due to the breach of trust. The idea here is understood to be in breaching the trust, rather than looking to any perceived harm to any applicable to situations where there is a former fiduciary relationship between the source of information and the insider. So the

Pre-existing relationship raises an obligation of trust and this justified regulation insider trading. A person can only be held liable if he is a fiduciary but a considerable number of those likely to deal while in possession of insider information are not in a fiduciary relationship. So the obvious problem here is that a person can be an insider if he has access to the insider information of the information is passed to him from an insider source. Therefore, the question is can liability arises where there who misuse insider information are not fiduciary? Although the fiduciary, represents a logical ground for the liability of fiduciary, it is limited as an approach for regulating other forms of insider trading. In the US, Common Law development has been directed to legislation. Regulating insiders trading in the US has been developed by the SEC and judicial precedents. The major problem has been finding the ground for liability for those ‘outside’ the corporation who misuse inside information. Therefore, different legal theories have been used to determine the definition of insiders and therefore to apply accepted legal norms.

**2.7 MISAPPROPRIATION THEORY**

Another theory which could come as a ground for the regulation of insider trading is the misappropriation theory which is the current position in the US. The regulation of insider trading her is justified on the basis that if regards information as property of the issues of the securities. Any person’s use of the information for his or another person’s benefits would amount to contradicting the owner’s interests. Therefore, insider trading is a misappropriation of the inside information which is the property of its source. However, the inside information will only be considered in the US as a property when it is misappropriated in breach of a fiduciary relationship. Accordingly, the idea in this approach is not that nor only the misuse of information is a jurisdiction for liability, the information and the capacity in which was used should be determining factor. This indicates that in order to holds an individual not to misuse the information. This obligation is normally founded on a fiduciary relationship, but the fiduciary relationship here is slightly different. The ‘insider’ need not owe the duty to the other party with whom he deals, nor has he owe the duty tot eh issuer of the subjected securities. The duty is owed to the source of eh information. There is a second explanation for such duty. Here the obligation is attached to anyone who possess the information knowing that its transfer is in breach of a fiduciary obligation not to misappropriate it. The misappropriation theory brings into question the legal issue of considering information as property. However, recognizing information as property has been criticized on the grounds which should also be available to the public. However, the principle that inside information has to be disclosed is not absolute.

There are situations in which the law allows non-disclosure, e.g. If it is for the benefit of the issuer. It has been observed that the recognition of information as property is important to sustain the misappropriation theory. However, assuring that the issue of property right or information is solved, there still arises the problem of determining the issues of ownership and possession. Misappropriation theory is criticized because it assigns ownership of nonpublic information to an employee or principal, and ignores the wider range of relationships. This suggests that the public shareholder may also have a right to such information.

The main problem of this theory is that it does not shows the important for the protection of the other party in the transaction in regards to dealing in a market. It also provides no answer regarding the information of disclosing material non-public information to the other party in the transaction. Therefore, pays no attention to the real reason behind regulating insider trading.

**CHAPTER THREE**

**THE REGULATION OF INSIDER TRADING IN NIGERIA**

The regulation of insider trading started as a result of the great danger which unrestricted use of inside knowledge can cause in dealings in company securities. Insider trading was not treated as a statutory offence in Nigerian until 1990. The more towards the regulation of insider trading in Nigeria was orchestrated by the Nigerian laws reform commission. The commission acknowledged that insider trading in was a serious malpractice[[33]](#footnote-32). The recommendation of the commission led to the commitment of provision on insider trading prohibition in sections 614 to 620 of the companies and Allied Matters Act 1990[[34]](#footnote-33) which used to be the pioneering provision containing the prohibitions of insider trading in Nigeria. The provision were copied from the English Company Securities (Insider Dealing) Act 1985.

The aforementioned provisions of CAMA turned out to be inadequate and inefficient for purpose of combating insider trading because for almost ten years after its inception, no person was successfully prosecuted under those sections. Consequently, the provisions under CAMA were repealed and replaced by sections 81 to 98 of the Investment and Securities Act 1999. The 1999 Act has now been repealed and replaced by sections 105 to 116 of the Investment and Securities Act 2007.[[35]](#footnote-34)

Apart from the above mentioned laws, there are some institutions that have emerged which are in one way of the other concerned with securities of companies. These institutions have come up with laws regulating dealing in these securities.

**3.1 OTHER INSTITUTIONS REGULATING INSIDER TRADING**

**3.1.1 The Securities and Exchange Commission**

This body was established by **section 1 (1) of ISA 2007**. The commission is a body corporate with perpetual succession and a common seal and may sue and be such in its corporate name. the functions and power of the commission are clearly set out in **5.13 of the Act** which include the regulation of investment and securities business in Nigeria as defined in the act; to regulate all offers of secondaries by public companies and entities; to facilitate the establishment of a nationwide system for securities trading in the Nigerian capital market in order to prevent investors and maintain fair and orderly markets; prevent fraudulent and unfair trade practices relating to the securities industry; to protect the integrity of the securities market against all forms of abuses including insider dealing, etc.

The commission may, from time to time, make rules and regulations for the purpose of giving effect to the provisions of the Act.[[36]](#footnote-35) In accordance with which we now have the Securities and Exchange Commission Rules and Regulations.

**3.1.2 The Nigerian Stock Exchange**

This body took over from the Lagos Stock Exchange in 1977. It is rules designed to check the misuse of inside information for share acquisition. These rules mainly regulate the behaviours of stock brokers in their dealing amongst themselves, with investors and the exchange itself. One of such is the requirement that a company can only be listed with the exchange if it satisfies the conditions set out in the listing requirement” such listed companies must ensure that investors, get good value for their money put into their shares. Thus they must make sure that all price sensitive information are published as quickly as possible and also enter into covenant to provide the exchange and the investing public with material information about their activities at the time of seeking and thereafter for retaining listing.

**3.1.3. Regulation by Other Financial Institutions**

A good example of these financial institutions is the bank, and there are laws regulating insider trading within them, one of such laws is the provision of the **Banking and Other Financial Institution Act** which, in the relevant section, provide for the directions of a bank to disclose their interest whatsoever, if they have any interest with respect to an advanced loan, or credit facility, or a proposed advance loan or credit facility from a bank. A similar provision is contained in the banking Act.

**3.2 COMPANIES AND ALLIED MATTERS ACT**

**Section 615 of CAMA** prohibits insiders from buying or selling of otherwise dealing in the securities of the company not offered to the public for sale or subscription. They are prohibited from dealing only in public companies. It appeared that insiders were only prohibited from dealing in the securities of public companies, but some other prohibited persons were prohibited from dealing in both private and public companies and this is irrespective of the fact that most companies in Nigeria are private companies. A was not clear why there was this dichotomy between the two classes. The fact that most companies in Nigeria are private companies ought to have warranted an extension of the provision to cover private companies as well.[[37]](#footnote-36)

The act of counseling or prouning another person to deal on communicating confidential involvement was restricted to dealing on a stock exchange. So, although the provisions applies to all prohibited persons, it last only as long as the deal is on a stock exchange. This would mean that even though tippees could not deal in the securities of a private company, they were not prohibited from passing the information to a third party to act on. The fine for this act of insider trading was considered meager and would not have defended anyone from committing the act of insider trading.

In order that a ground for insider dealing be established, the plaintiff must have concluded a transaction of sale or purchase. No liability would arise even if it was shown that revelation of the confidential information would have induced a reluctant outsider to conclude the transaction. Civil liability only subsists for two years from the date of the completion of the transaction that gave rise to the course of action. A shroud insider may be able to evade liability by shielding the transaction for the length of time. Corporate recovery is based on the breach of a fiduciary duty owed by the insider to the company. Where the insider has already compensated the other party for the direct loss suffered, the company can no longer sue him for the profits realized on the transaction for then it would no longer be part of the direct benefits or advantages realized from the transaction.

**3.3.1 Primary Insider Trading – Acts Prohibited**

**Section 111 (1) ISA** provides that a person who is an insider of a company shall not buy or 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.

It should be that the act prohibited here relates only to trading in securities which are offered to the public, for example, dealings on approved securities exchange or capital trade point. It appears from the statutory provision that dealing in securities of private companies are exempted from prohibition. The individual must deal whilst in possession of inside information. It is not necessary for the prosecution to establish that the inside information was actually used by the insider in arriving at his decision to deal. This arises by implication from the fact of possession and dealing. The individual must hold the information by virtue of being connected with or having being connected with the relevant company.

In practice, this means that the prosecution must show that the individual obtained inside information through his special access or relationship with the company. Specification of information is very important because the more specific it is the less risk the insider takes by acting upon it. Therefore it must not be one of a general nature relating to or concerning the company. The information will be such that if it were generally known to person.

Price sensitive information in relation to those securities who are accustomed or would be likely to deal in those securities, it would be likely to materially affect the price of those securities.

The offence requires proof of deliberate abuse of position by engaging in insider trading. The prosecution must establish that the individual acted intentionally is at least recklessly in relation to all the elements of the offence. That is;

1. He must know that he is or has been connected with a company;
2. He must know that the information is unpublished price sensitive information in relation to the relevant securities;
3. He deals in those securities on a recognized stock exchange or through an investment exchange.

**3.3.2 SECONDARY INSIDER TRADING**

The Act envisaged a situation where insider trading can occur outside primary insiders like the directors of a company, officers and employees, it consequently made a provision prohibiting those who are not primary insider from engaging in insider trading.

**3.3.2.1 TIPPEE**

The ISA prohibits an outsider (a tippee) from trading with information obtained from an insider. **Section 111 (2)** extended the prohibition imposed on primary insiders to secondary insider by stating that **s. 111(1)** applies where a person (a tippee) has information which he knowingly obtains (directly or indirectly) from another person who:

1. Is connected with a particular company, or was at any time within the six months preceding the obtaining of the information, so connected;
2. The former person (the tippee) knows about, or has reasonable cause to know that the later person (the insider) holds, the information by virtue of being so connected; and
3. The tippee knows or has reasonable cause to believe that, because of the insider’s connected and position, it would be reasonable to expect him not to disclose the information except for the proper performance of the function attached to that position.

In such circumstances **s. 111(3)** provides that the tippee;

1. 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; and
2. Shall not himself deal in securities of any other company if he knows that the information is unpublished price sensitive information in relation to those securities and it relates to any transaction (actual or contemplated) and 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.

A tippee is also prohibited from dealing in a company’s securities if he has knowingly obtained unpublished price sensitive information from a person who contemplates or is no longer contemplating a take over offer.[[38]](#footnote-37) There is also a similar prohibition against a tippee who knowingly obtained any such information from a public officer or homes public officer.[[39]](#footnote-38)

**3.3.2.2 Counseling or Procuring Dealings in Securities**

Under s. III (6) a person who is for the time being prohibited by the provision of s. III from dealing on an approved securities exchange or capital trade point in any securities shall not counsel or procure any other person to believe that the person would deal in those securities.

It has been submitted that category of dealers prohibited under s. 111(6) are the insiders under s.III who deal in the securities of his own company which are offered to the public for sale or subscription. It appears that this provision is contravened as long as counseling or procuring is established. It is immaterial counseled or procured does not afterwords deal in the securities, provided the counselor or procures knows or has reasonable cause to know that he would deal in the securities. This is a structurability provision.

**3.3.3 OTHER TYPES OF INSIDER TRADING**

**3.3.3.1 Abuse of Information Obtained in Official Capacity**

This relates to information held by a public offices or former public officers. Section 112 applies to any information which:

1. Is held by a public offices or former public offices by virtue of his position or former position as a public officer, or is knowing obtained by a person (directly or indirectly) from a public offices or former public offices who he knows or has reasonable cause to believe held the information by virtue of any such position;
2. It is reasonable to expect of person in the position of a public offices or former position of a public offices not to disclose except for the proper performance of the functions attaching to that position; and
3. The person holding it known it is unpublished price sensitive information in relation to securities of a particular company, which is referred to as “relevant securities”.

A public officer holding such information as explained herein before and any individual who knowingly obtains such information from such public officer or former public officer is not allowed to deal in any “relevant securities” nor counsel or procure any other person to deal in the securities, knowing or having reasonable cause to believe that such person would deal in the relevant securities.[[40]](#footnote-39) Such person i.e. the public officer or individual as describes above are also prohibited from communicating to any others person information held or obtained respectively.[[41]](#footnote-40)

Pursuant to s. 112 (4) if it appears to the securities and Exchange Commission that the members, officers or employees of or persons otherwise connected with any body by appearing to it to exercise public functions may have access to unpublished price sensitive information relating to security, the commission may declare that those persons are public officers for the purpose of **s. 112**. The term “public officer” means any person working in the public service of the federal or of a state as defined in the constitution of the Federal Republic of Nigeria.

**3.3.3 Insider Trading in a Take-Over Bid**

The Act forbids a person contemplating a take over offers in securities in different capacity from dealing in those securities accordingly **S. 111(4)** specifically provides that:

“Where a person is contemplating or has contemplated making (with or without another person) a take –over other. For a company in a particular capacity, that person shall not deal in securities or that company in another capacity if he knows that the other is unpublished price sensible information I relation to those securities”

The prohibition here seems to extend to dealing in securities of private companies as no reference is made to “securities which are offered to the public for sale of subscription”.

**3.3.4 Actions Not Prohibited**

Just like any general rule is limited by its exceptions, the low regulating insiders trading is no exception. Under **S. 113,** a number of exceptions are made to the prohibition of insider trading as contained in **Sections 111** and **112 of the Act.** The following acts which are excepted seems not to another to insider trading under the act.

The first exception is to the found in **paragraph (a) of S. 13.** It provides that doing any particular thing otherwise than with a view to the making of a profit or the avoidance of a loss (whether for himself or another person) by the use of that information.

The onus is on the defendant neither to establish that he used the information for a purpose which is neither for profit making nor to avoid a loss. It is however difficult to envisage the circumstances where a deal would not be in part of least for the purpose of making of profit or the avoidance of a loss.

Another exception is that a person is not prohibited from entering into a transaction in the course of the exercise in good faith of his functions as a liquidator receiver or trusted in bankrupting. The exception is enacted in **paragraph (b) of S. 113.** In so fat as the deal is entered into in the course of the exercise in good faith of their function, they are placed outside the scope of the prohibition on insider trading.

By **S. 113 (c)** a person is not prohibited from doing any particular thing if the information was obtained by him in the course of a business of a stock brothers in which he was engaged or employed or 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. In a similar rein, doing any particular thing in relation to any particular securities, if the information was of a description which it would be reasonable to except him to obtain in the ordinary course of that business and he does prohibited.[[42]](#footnote-41)[1]

These provisions afford protection to recognized dealers in company securities. The effect of the provision is to allow a person concerned with the particular transaction in the relevant security where the dealing is done in order to facilitate the completion or carrying out of that transaction. At the same times, the provision permits an individual within the scope of the prohibition contained in the relevant section to counsel, procure or communicate relevant information to others, provided that such is done in order to facilitate the completion or carrying out of the transition.

**3.3.5 Criminal Liability Under The Act**

If an offence is created without an attendant punishment, then the likelihood of not committing the offence will not be there. There **Section 115** provides that any person who contravenes any of the provisions of the Act regulating trading inn securities commits an offence and is liable on conviction:

1. In the case of a person not being a body corporate, to line of not less than N500,000 or an amount equivalent to double the amount of prohibit delivered by him or los averted by the use of the information obtained in contravention for a term not exceeding seven years, or
2. In the case of a person being a body corporate to a line not less than N1,000,0000 or an amount equivalent to twice the amount of profit delivered by it or loss averted by the use of the information obtained in contravention of any of the provisions of this part.

A person who is liable under part XI shall pay compensation at the order of the commission or the Tribunal, as the case may be, to any aggrieved person who, in a transaction too the purpose or sale of securities entered into with the first-mentioned person or with a person acting too or on his behalf, suffers a loss by reason of the different 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.[[43]](#footnote-42)[2] The amount of compensation for which a person is liable under **S. 116(I)** is the amount of the loss sustained by the person charming the compensation or any other amount as maybe determined by the commission on the Tribunal[[44]](#footnote-43)[3].

It is noteworthy that any transaction in contravention of **S. 111 or 112** is avoidable at the instance of the Commission[[45]](#footnote-44)[4]

**CHAPTER FOUR**

**A COMPARATIVE ANALYSIS OF THE CONCEPT OF INSIDER TRADING IN NIGERIA WITH SOME OTHER JURISDICTIONS**

The rules governing insider trading are complex and very significantly from country to country.[[46]](#footnote-45) The content of enforcement also varies from one country to another. The definition of insider in one jurisdiction can be broad, and may cover not only insider themselves but also any person related to them, such as brokers, associates and even family members.

**4.1 UNITED STATES INSIDER TRADING LAW**

The Unite State has been the leading country in prohibiting insider trading made on the basis of material non-public information. They are generally viewed as having the strictest laws against illegal insider trading, and make the most serious efforts to enforce the laws.[[47]](#footnote-46) Insider trading in the U.S has a base offense level of 8, which puts it in Zone A under the U.S Sentence Guidelines. This means that first time offenders are eligible to receive probation rather than maceration.

**4.1.1 STATUTORY LAW**

The U.S insider trading prohibitions are based on English and American common law prohibition against fraud. In 1909, well before the **Securities** **Exchange** **Act** was passed, the United States Supreme Court ruled that a corporate director who bought that company’s stock when he knew the stock’s price was about to increase committed fraud by buying but not disclosing his inside information.[[48]](#footnote-47)

**Section 15 of the U.S Securities Act 1933** contained prohibitions of fraud in the sale of securities which were greatly strengthened by the **Securities Exchange Act of 1934. Section 16(b) of the Securities Exchange Act 1934** prohibits short – swing profits (from any purchases and sales within any six – month period) made by corporate directors, officers, or stockholders owing more than 10% of a firm’s shares. Under s**. 10(b) of the 1934 Act, SEC Rule 10b-5** prohibits fraud related to securities trading.

The **Insider Trading Sanctions Act of 1984** and the **Insider Trading and Securities Fraud Enforcement Act of 1988** place penalties for illegal insider trading as high as three times the amount of profit gained or loss avoided from the illegal trading.

**SEC Regulation F.D (“Fair Disclosure”)** requires that if a company intentionally discloses material non-public information to one person, it must simultaneously disclose that information to the public at large. In the case of an unintentional disclosure of material non-public information to one person, the company must make a public disclosure “promptly”. Insider trading, or similar practices, are also regulated by the SEC under its roles on takeovers and tender offers under the **Williams Act**.

**4.1.2 U.S Court Decisions**

Much of the development of insider trading law has resulted from court decision. In **SEC v. Texas Gulf Sulphur Co.**[[49]](#footnote-48), a federal circuit court stated that anyone in possession of inside information must either disclose the information or refrain from trading. Officers of the Texas Gulf Sulphur Corporation had used inside information about the discovery of kidd mine to make profits by buying shares and call options on company stock.

In 1909 the Supreme Court of the United States ruled in **Strong v. Repide**[[50]](#footnote-49) that a director who expects to act in a way that affects the value of shares cannot use that knowledge to acquire shares from those who do not know of the expected action. Even though in general, ordinary relations between directors and shareholders in a business corporation are not of such a fiduciary nature as to make it the duty of a director to disclose to a shareholder the general knowledge which he may posses regarding the value of the shares of the company before he purchases any from a shareholder, yet there are cases whereby reason of the special facts, such duty exists.

In 1983 the U.S. Supreme Court ruled in the case of **Dirks v. SEC**[[51]](#footnote-50) that tippees are a fiduciary duty in disclosing confidential information and the tipper received any personal benefit from the disclosure. In Dirks, the “tippee” received confidential information from an insider, a former employee of a company. The reason the insider disclosed the information to the tippee, and the reason the tippee disclosed the information to third parties, was to blow the whistle on massive fraud at the company. As a result of the tippee’s efforts the fraud was uncovered and the company went into bankruptcy. But. While the tippee had given the “inside” information to clients who made profits from the information, the U.S Supreme Court ruled that the tippee could not be held liable under the federal securities laws for the simple reason that the insider from whom he received the information was not releasing the information for an improper purpose (i.e. a personal benefit), but rather for the purpose of exposing the fraud. The court ruled that the tippee could not have been aiding and abetting a securities law violation committed by the insider – for the simple reason that no securities law violation had been committed by the insider.

In **Dirks,** the Supreme Court also defined the concept of “constructive insider”, who are lawyers, investment bankers and others who receive confidential information from a corporation while providing services to the corporation. Construction insider are also liable for insider trading violation if the corporation expects the information to remain confidential, since they acquire the fiduciary duties of the true insider.

The next expansion of insider trading liability came in **SEC v. Materia**[[52]](#footnote-51), the case which first introduced the misappropriation theory of liability for insider trading. Material, a financial printing from proof reader, and clearly not an insider by any definition, was found to have determined the identity of takeover targets based on proofreading tenders offer documents during his employment. The second Circuit Court of Appeals hold that the theft of information from an employer, and the use of that information to purchase or sell securities is another entity, constituted a fraud in connection with the purchase or sale of securities. The misappropriation theory of insider trading was born, and liability furthers expanded to encompass a larger group of outsiders.

In case of United States v. Carpenter the U.S Supreme Court cited an earlier ruling while unanimously upholding mail and wire fraud convictions for a defendant who received his information from a journalists rather than from the company itself. The journalist, R. Foster Winans, was also convicted on the grounds that he had misappropriated information belonging to his employee, the Wall Street Journal. In that widely publicized case, Winans traded in advance of “Heart on the Street” columns appearing in the journal.

The court stated in Carpenter: “It is well established , as a general proposition, that a person who acquires special knowledge of information by virtue of a confidential or fiduciary relationship with another is not free to export that knowledge or information for his own personal benefit but must account to his principal; for any profits derived therefrom”. However, in upholding the securities fraud (insider trading) convictions, the justices were evenly split.

In 1997 the U.S Supreme Court adopted the misappropriation theory of insider trading in **United States v. O’Hagan**.[[53]](#footnote-52) O’Hagan was a partner in a law firm representing Grand Metropolitan, while it was considering a tender offer for Pillsbury Company. O’Hagan used this inside information by buying call options on Pillsbury stock, resulting in profits of over $4.3 million. O’Hagan claimed that neither he nor his firm owed a fiduciary duty to Pillsbury, so he did not commit fraud by purchasing Pillsbury options. The court rejected O’Hagan’s arguments and upheld his conviction.

The “misappropriation theory” holds that a person commits fraud “in connection with” a securities transaction and thereby violates 10 (b) and Rule 10 b – 5, when he misappropriates confidential information for securities trading purposes, in breach of a duty owed to the source of the information. Under this theory, a fiduciary’s undisclosed, self-serving use of a principal’s information to purchase or sell securities in breach of a duty of loyalty and confidentiality, defrauds the principal of the exclusive use of the information. In view of premising liability on a fiduciary relationship between company insider and purchases or seller f the company’s stock, the misappropriation theory premises liability on a fiduciary – turned – trader’s deception of those who entrusted him with access to confidential information.

The court specifically recognized that a corporation information is its property: “A company’s confidential information… qualifies as property to which the company has a right of exclusive use. The undisclosed misappropriation of such information in violation of a fiduciary duty … constitutes fraud similar to embezzlement – the fraudulent misappropriation to one’s own use of the money or goods entrusted to one’s care by another”.

In 2000, the SEC enacted SEC Rule 10b5-1, which defined trading “on the basis of” inside information as any time a person trades while aware of material non public information. It is no longer a defense for one to say that one would have made the trade anyway. The rule also created an affirmative defense for pre – planned trades.

In 2014, in the case of United States v. Newman,[[54]](#footnote-53) the United States Court of Appeals for the second circuit cited the Supreme Courts decision in **Dirks**, and ruled that in order for a “tippee” (i.e. a person who has received insider information from an insider aid has used that information) to be guilty of insider trading, the tippee must have been aware not only that the information was insider information, but must also have been aware that the insider released the information for an improper purpose (such as personal benefit). The court concluded that the insider’s breach of a fiduciary duty not to release confidential information in the absence of an improper purpose of the part of the insider is not enough for criminal liability to be imposed on the either the insider or the tippee.

**4.2 UNITED KINGDOM INSIDER TRADING LAW[[55]](#footnote-54)**

The prohibition of insider trading in Britain started with a “joint statement” issued in 1973 by the Stock Exchange and the Takeover Panel which called for criminal sanction against insider trading. The term insider dealing has been used in British law since 1980. After several aborted tries to pass legislation through the parliament, on 23 June, 1980, **section 69-73** contained in part v of the **Companies Act 1980** came into force and made “insider dealing” a criminal offence. Later on this was re-enacted in the **Company Securities (Insider Dealing) Act 1985**. After suggesting the reform of law, dealing with the investment industry in a white paper, insider trading was amended by the **Financial Services Act 1986**. Further impulse for the next reform in the U.K. came in 1989, in order to comply with **European Commonly Directive 89/592/EEC (Insider Dealing)**, which was aimed to co-ordination of the insider trading in the member states. The companies Securities (Insider Dealing) Act 1985 was repealed and replaced on 1st March, 1994 by **section 52 to 54 of the Criminal Justice Act 1993**, implementing the above mentioned directive. Presently in the U.K, **Part V of the Criminal Justice Act 1993**[[56]](#footnote-55)deals with insider dealing wherein are contained several forms on insider trading which makes them criminal offences.

**4.2.1 Financial Services and Markets Act 2000 and FSA’s Model Code**

As we can see, the problem of insider dealing is contained in criminal law and can also be sanctioned by civil law under the control of the Financial Services Authority (FSA). The FSA is an independent and non-governmental organization whose authority is based upon Part VI of the Financial Services and Market Act 2000 (FSMA). The FSMA introduced the broader offence of market abuse which includes insider dealing, disclosing inside information, dissemination of false and misleading information and employing fictitious devices. All of these offences are included in the term “Insider dealing”.

The FSA is a securities regulator focused on the companies which issue the securities traded in financial markets. It is a company limited by guarantee and financed by the financial services industry. The FSA’s model code, which is adopted in chapter 9 of the Listing Rules and contain “discharging managerial responsibilities”, which listed companies are required to adhere. This is a model, which all listed companies have to adopt as they are required to take “all proper and reasonable” actions to meet criteria contained in the model code. The model code is not directly binding for directors of a listed company, but the company has to adopt this code. Possible breach of the adopted code is a breach of the duty owed by the directors to the company, not to the FSA. The duty owed by the company to the FSA is to adopt the code itself.

The main restriction included in the model code are;

1. A director must not deal in securities within a period of 60 days preceding the preliminary announcement of the final results. Similar rule applies to half year and quarterly results.
2. A director must not deal at any time when he or she knows price sensitive information, which has not been published. The price sensitive information is any information, which is able after the publishing to have a demand on the value of the respective securities.
3. A director must seek clearance from the chairman (or other directors designated by the board for this purpose prior to entering into the transaction.
4. Clearance to deal in any securities must not be given during a prohibited period, it is during a period when price sensitive information is unpublished but is known.

**4.4.2 Criminal Justice Act 1993**

Protection under the **Part V of the Criminal Justice Act 1993** consists of three criminal offences which can commit an individual are described in **s. 52** and they are;

1. An insider who disposes information is guilty of insider dealing if, under the specified circumstances, he deals in securities and provided that the information is made public, would then have had a significant effect on the price of the securities (price – affected securities).
2. An insider encourages another person to deal in such securities, knowing or having reasonable cause to believe that other would do so.
3. An insider discloses the information beyond that if the proper performance of the functions of his employment, office or profession, to another person.

In accordance with these three offences, an insider can be sentenced up to seven years imprisonment and can also be tried. Under **s.63 (2)** is stated that, no contract shall be void or unenforceable, because of the fact that an offence was committed.

The difference between the CJA and the FSMA is simply that the CJA contains criminal liability for insider trading but does not contain a civil remedy but the FSMA established civil sanctions to supplement the CJA.

**4.3 A COMPARISON OF INSIDER TRADING REGULATION IN US, UK AND NIGERIA**

The U.S has been the leading country in prohibiting insider trading made on the basis of material non public information. The regulation started in 1909 in the case of **Strong v. Repide**. In 1933 they had already made a law prohibiting fraud in the sale of securities.[[57]](#footnote-56) The prohibition of insider trading in the U.K. can be traced to the 1980 **Companies Act** following a joint statement issued in 1973 by the Stock Exchange and the Takeover Panel which called for criminal sanction against insider trading in Nigeria, on the other hand, can be traced to the **Companies and Allied Matter Act of 1990** following the recommendation of the Nigerian Law Reform Commission.

The U.S has plethora of laws on the regulation of insider trading and they include the Securities Act of 1993, the Securities and Exchange Act of 1934, the Insider Trading Sanctions Act of 1984, the Insider Trading and Securities Fraud Enforcement Act of 1988 and the SEC Rules. The same may be said of U.K but in Nigeria we have the Investment and Securities Act 2007 and the SEC Rules.

The self-regulation is the dominant regulatory system in the U.S but under thorough monitoring by he SEC. Statutory regulation is dominant in U.K and Nigeria.

In the U.S, for purposes of the regulation of insider trading, it is not required that the securities be traded or listed on an exchange. In the U.K, the securities must have been listed on the U.K Stock Exchange and the most difficult thing about proving insider dealing in the U.K is that the act must have been carried out while the culprit was in the U.K. In Nigeria, on the other hand, the prohibition of insider trading applies to trading in the securities of any company listed on the Nigeria Stock Exchange. However, it is immaterial whether the transaction was conducted outside Nigeria or that the insider is resident outside Nigeria.

**CHAPTER FIVE**

**CONCLUSION AND RECOMMENDATION**

**5.1 CONCLUSION**

The prohibition of the concept of insides trader is orchestrated by moral, social and economic consideration. Various countries of the world have enacted laws and also established commissions to regular insider trading. The United States of America obviously is at the forefront of the light against this concept and they are closely followed by the United Kingdom. This was made possible by the relentless effort of those in charge of its regulation. In the aforementioned countries, the judiciary has contributed in no small measure towards the development of inside trading laws. Those saddled with the responsibility of enforcing the law are alive in their duties.

It is unfortunate that in Nigeria there has been conviction on insider trading. Does it then man that insider trading does not occurs in Nigeria? The answers will certainty in the negative. Nigeria has the laws; even though the laws have not been tested in eh law whether they are adequate. Otherwise it seems that Nigerians problem with respect to inside trading has been the enforcement of the laws. The maze existence of inside trading regulation is not sufficient to assure optimal securities market development; enforcement of insider trading regulation is the key. A law that lacks a probability of enforcement is an ineffective law. There are several factors which inhibit the effective enforcements of insider trading regulation in Nigeria. Some of them will be discussed.

The civil remedies contain S. 116 ISA 2007 is in adequate and ineffective to curb insider trading in Nigeria. The provision only enables a person to claim compensation on the order of SEL so the investment and securities Tribunal establishment under S. 274 ISA is grossly deficient since it is too limited in score as it only provides compensations. It does not also give the victims of insider trading the right to institute private civil action before a regular court of competent jurisdiction.

Another factor identified is the investigation of insider trading. For there to be effective investigation of insider trading infractions, the regulatory body must have wide powers of investigation. The SEC in the US has the power to investigate cases of insider trading to take depositions and to summon witnesses. It can also search for and since documents which are relevant to the investigation. In Nigeria, the SEL is not endowed with such powers.

Many investors are still not aware of insider trading let alone the negative consequences it may have on them and the economy. Several investors lack the business sophistication that would make them concerned with or even understand the concept of insider trading. This goes to show that there is lack of awareness of the concept in Nigeria.

**5.2 RECOMMENDATION**

It sis recommended that the SEC and NSE, in conjunction with relevant market operators should develop a clear-out regulations specifically relating to insider trading as a prelude to renewed champ down on violations promogation and strict enforcement of requirements for mandatory disclosure of material information by quoted entities should be mode and the SEC alongside NSE should ensure more rigorous monitoring of transactions on the floor of the Nigerian stock exchange.

Adequate awareness and education of insider trading offences to all relevant patrons should be made. Awareness and educational strategies are important to ensure that the public is aware of those rights. The ISA should be amended to empower the SEC carrying out the investigation necessary his an insider trading prosecution. The question of investigation is of the core of effective enforcement of the regulations and until the problems of detection and investigation are properly addressed attempts to prohibit insider trading will remain illusory.

The ISA should be amended to categorize a company and every shareholder as an insider. At the same time, the securities of unlisted public company as well as that of a private should be included in the prohibited securities.

1. See generally Regulation of Insider Trading/Law Teacher<http://www.lawteacher.net/free-law-essays/trading-law/regulation-of-insider-trading-law-essays.php> accessed on 10 April, 2010 [↑](#footnote-ref-0)
2. J. H. Thompson, ‘A Global Comparison of Insider Trading Regulations’ (2014=30 IJAFR. V 311 1 [↑](#footnote-ref-1)
3. *Ibid* [↑](#footnote-ref-2)
4. J. O. Orojo, Company Law and practice in Nigeria (5th Edu, Durban: Lexis Nexis, 2008) P. 390 [↑](#footnote-ref-3)
5. *Ibid* [↑](#footnote-ref-4)
6. J. H> Thompson, ‘A Global Comparison of Insider Trading Regulations’ (2013) IJAFR. V3:1 1 [↑](#footnote-ref-5)
7. *Ibid*  [↑](#footnote-ref-6)
8. A Garba, ‘Impediments to Effective Enforcement of Insider Trading Regulations in Nigeria’ (2013) IJM 13 [↑](#footnote-ref-7)
9. J. O. Orojo, Company Law and Practice in Nigeria (3rd edn, Lagos: Mbeyi and Associate, ) p.447 [↑](#footnote-ref-8)
10. See British Industrial Phastic v Ferguson 9(1938)4 ALL ER. 504 [↑](#footnote-ref-9)
11. Percial v Wright (1902)2 Ch. 421 [↑](#footnote-ref-10)
12. I. J. Essien, ‘A Gritical Examination of the statutory Bottleneck Against Insider Dealing’ (2007) NSLJ vol 2 145. [↑](#footnote-ref-11)
13. 213 US 419 (1909 [↑](#footnote-ref-12)
14. See Security Exchange Act 1934 (USA) S. 166 and Rules 106 -5 made by US SEC. [↑](#footnote-ref-13)
15. See report on the reform of Nigerian Company Law (1988/vol. 1 p.30 [↑](#footnote-ref-14)
16. Hereinafter referred to as the CAMA, the regulation of insider trading dates back to the enactment of CAMA. Section 614 – 620 was the pioneering provision which contained a prohibition on insider trading in Nigeria [↑](#footnote-ref-15)
17. Regrettably even under Investment and Securities Act 2007 Hereinafter referred as the 2007 ISA no successful conviction has been recorded for insider trading, the reason could be that most of eh flaws of the CAMA and ISA 1999 were simply carried over to the 2007. ISA. [↑](#footnote-ref-16)
18. Black’s Law Dictionary 9th edn p. 866 [↑](#footnote-ref-17)
19. *Ibid* p.1634 [↑](#footnote-ref-18)
20. *Ibid* p.1476 [↑](#footnote-ref-19)
21. *Ibid* p. 1621 [↑](#footnote-ref-20)
22. *Ibid* [↑](#footnote-ref-21)
23. See generally V Chauhen et al ‘Insider Trading, market Efficiency, and Regulation. A Literature Review’ RFB vol 06 Issue 1 2014. [↑](#footnote-ref-22)
24. ‘The Insider Dealing’ (2016) <http://www.lawteacher.net/free-law-dissertations/criminal-law/insider-dealing.php> accessed on 5 May, 2016 [↑](#footnote-ref-23)
25. This latter view has been less heard of late [↑](#footnote-ref-24)
26. H.G Manne, Insider Trading and the Stock Market (New York: Free Press, 1966) [↑](#footnote-ref-25)
27. 40 S.E.C. 907, 1961 WL 3743 (1961) [↑](#footnote-ref-26)
28. 401 F. 2d 833 (2nd Circuit, 1968) [↑](#footnote-ref-27)
29. J. Moore, ‘What is Really Unethical about Insider Trading?’ (1990) JBE vol.9 Issue 3, 171 [↑](#footnote-ref-28)
30. D.W Carlton and D.R Fischel, ‘The Regulation of Insider Trading’ (1982) 35 SLR 857 [↑](#footnote-ref-29)
31. B Rider and H L Frrench, ‘The Regulation of Insider Trading (1979) 263 [↑](#footnote-ref-30)
32. S.M Bainbridge, ‘Insider Trading: An Overview’ (1998) <http://papers.ssrn.com/5013/papers.cfm?abstract_id=132529> accessed on 8 April, 2016. [↑](#footnote-ref-31)
33. See report on the Reform of Nigerian Company Laws (1988)vol. 1 p.30 [↑](#footnote-ref-32)
34. Hereinafter referred to as CAMA [↑](#footnote-ref-33)
35. Hereafter referred to as ISA 2007 [↑](#footnote-ref-34)
36. See generally s. 313 of ISA 2007 [↑](#footnote-ref-35)
37. See generally The Insider Dealing <http://www.lawteacher.net/free-law-dissertations/criminal-law/insider-dealing.php>> accessed on April 30, 2016 [↑](#footnote-ref-36)
38. S. III (4) ISA [↑](#footnote-ref-37)
39. S. N.2 (2) [↑](#footnote-ref-38)
40. S. 112 (2) and (3) (a) & (b) [↑](#footnote-ref-39)
41. S. 112 (3) (c) [↑](#footnote-ref-40)
42. [1] See **S. 113(d)**  [↑](#footnote-ref-41)
43. [2] S. 11(1) [↑](#footnote-ref-42)
44. [3] S. 116(2) [↑](#footnote-ref-43)
45. [4] S. 114 [↑](#footnote-ref-44)
46. See generally Insider trading – Wikipedia the free encyclopedia[https://en.m.wikipedia.org/wiki/Insider-trading#cite\_note-4](https://en.m.wikipedia.org/wiki/Insider-trading" \l "cite_note-4) accessed on 21 April, 2016. [↑](#footnote-ref-45)
47. J. C. Coffee ‘Law and the Market: The Impact of Enforcement’ (2007) Columbia Law and Economics Working Paper No. 304. [↑](#footnote-ref-46)
48. That was in the case of Strong v. Repide 213 US 419 (1909) [↑](#footnote-ref-47)
49. 401 F. 2d 833 (2d Cir. 1968) [↑](#footnote-ref-48)
50. 215 U.S. 419 (1909): Justia U.S. Supreme Court Centre [↑](#footnote-ref-49)
51. 463 U.S. 646 (1983) [↑](#footnote-ref-50)
52. 745 F. 2d 197 (2d Cir 1984) [↑](#footnote-ref-51)
53. U.S 642, 655 (1997) [↑](#footnote-ref-52)
54. 773 F.3d 438 (2d Cir. 2014) [↑](#footnote-ref-53)
55. See generally Regulation of Insider Trading/Law Teacher<http://www.lawteacher.net/free-law-essays/trading-law/regulation-of-insider-trading-law-essays.php> accessed on 10 April, 2010 [↑](#footnote-ref-54)
56. S. 52 thereof described the three criminal offences [↑](#footnote-ref-55)
57. S. 15 of Securities Act 1933 [↑](#footnote-ref-56)