

LAW AND PRACTICE WITH RESPECT TO INSIDER TRADING AND TRADING ON MARKET INFORMATION IN THE UNITED KINGDOM

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At last insider trading in the U.K. is a crime! It took us nearly fifty years to catch up with the United States in this respect – but, you may say, that is par for the course in all aspects of our life. Until 1980 insider trading was in the province of the self-regulatory system: during the 1970s any sanction against an insider dealer was generally imposed by the Take-over Panel.

For many years there was a growing demand that the government should legislate to make insider dealing a crime. As long ago as February 1973, the Stock Exchange and the Take-over Panel advocated legislation. Due to a strange quirk of fate (two governments falling while Companies Bills were before Parliament) it took three attempts by government for the provisions to reach the statute book. The provisions on insider dealing contained in the Companies Act 1980 (sections 68–73) came into force on June 23, 1980.

The essential feature of the Act is that it makes it a crime for certain persons to breach faith by dealing in securities where they have “unpublished price-sensitive information”. These persons are individuals who are knowingly connected with a company at the time of dealing, or at any time in the preceding six months, and individuals who receive information from connected individuals (*i.e.* tippees).

Connected persons include directors, officers, or senior employees of the company and the company’s professional advisers. Shareholders of a certain percentage or more of shares in a company are not, *per se*, connected persons. Both a connected person and a tippee are prohibited not only from dealing but also from counselling anyone to deal or from communicating the unpublished price-sensitive information to anyone who might reasonably be expected to deal in the relevant securities. Individuals connected with one company are also prohibited from dealing on the basis of unpublished price-sensitive information in the securities of another company, if they have acquired the information because they are connected with the first company.

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The Act provides that an individual having unpublished price-sensitive information is not prohibited from "doing any particular thing otherwise than with a view to the making of a profit or the avoidance of a loss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". This defence is regarded as providing a necessary measure of protection in order not to discourage directors and employees from acquiring shares in their company. Although the evidentiary question may sometimes be a difficult one (a person who trades generally has some excuse, however implausible), such factors as trading at a time close to the announcement of price-sensitive information and departing from one's normal investment pattern will speak for themselves.

The Department of Trade will itself carry out investigations, although considerable reliance will be placed on the Stock Exchange to supply the necessary raw material. In the two years since June 1980, there have been three prosecutions. In two cases the accused pleaded guilty, and in the third the case has yet to be heard.

Some people have suggested that the legislation will have little effect on curbing whatever abuses exist. They believe that the inadequacy of the methods of enforcement and the scope for clandestine dealing behind the front of a foreign bank nominee make the legislation more symbolic than real. Nobody can ever know how much insider dealing takes place (in contrast to certain other crimes), so it will be impossible to judge the deterrent effect of the new law. But it is the deterrent effect that advocates of the legislation see as the main purpose of this law. If the experience of other countries – e.g. France, Australia, Singapore – is anything to go by, the chances of more than a few prosecutions in the next few years are remote. But, of course, the deterrent effect cannot be judged by this criterion.

Finally, a few words on the comparative aspect. In the United States, civil remedies have dealt with the problem for many years, and the criminal provisions have rarely been invoked. (note *Chiarella* and the recent Morgan Stanley case). Because of a different legal system (no class actions or contingency fees) and a different general ethos (a fairly non-litigious race), any U.K. legislation on the topic was bound to be based on criminal law. There are no statutory civil remedies created by the 1980 Act. As a matter of policy, there is no short-swing profit concept (Section 16(b) of your 1934 Act) in the Act, nor would the Act catch "scalping". Although both topics were discussed, I believe it was felt that the first attempt at legislation on the subject should not be too ambitious nor be guilty of the charge of overkill.

A final postscript: I believe *Chiarella* would have been found guilty under the 1980 Act, as he would have been under your new SEC Rule 14(e)-3, which seems to have quite a lot of features in common with our new Act. But to me as an outsider, the Rule, sadly, seems to apply only in the context of tender offers. Why is this?