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Regulation of Insider Trading in Nigeria

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Introduction

Insider trading occurs where a person, being in possession of some confidential and price sensitive information not generally available to the public, utilizes such information to trade securities for his own benefit. The premise for the prohibition of insider trading is the desirability of traders having equal access to information during trading.

Section 315 of the Investments and Securities Act 2007 ("ISA") defines an "insider" as any person connected with the company in any of the following ways:

a. a director of the company or a related company;
b. an officer of the company or a related company;
c. an employer of the company or a related company;
d. an employee of the company, involved in a professional or business relationship of the company;
e. any shareholder of the company owning five (5) per cent or more of any class of securities or any person who is or can be deemed to have any relationship with the company; or
f. members of the audit committee of a company.

In the old English case of ***Percival v. Wright*** (1902) 2 Ch. 421, the Court of Appeal clearly held that a director owed no fiduciary duty to a shareholder and therefore could purchase with impunity the latter's shares while in possession of favourable confidential information about the company. Due to the common law limitations and in a bid to protect investors adequately against insider trading, most jurisdictions make express provisions against market infractions such as insider trading.

Section 111(1) of ISA prohibits any person who is an insider of a company, from buying, selling, or otherwise dealing in the securities of the company, which are offered to the public for sale or subscription if he has unpublished price-sensitive information in relation to those securities.

Section 111(2) of ISA further prohibits any person from buying, selling or otherwise dealing in the securities of the company, which are offered to the public for sale or subscription where:

a. such a person has information, which he knowingly obtains (directly or indirectly) from another person who is connected with a particular company, or was at any time within the six months preceding the obtaining of the information so connected;

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b. where the former person knows or has reasonable cause to believe that, because of the latter's connection and position, it would be reasonable to expect him not to disclose the information except for the proper performance of the functions attached to that position.

Section 111(3) further extends the prohibition against the use of *unpublished price-sensitive information* to a wider range of circumstances.

Information plays a crucial part in investment decisions. Share prices should reflect all available information affecting important investment decisions; hence, regulatory authorities impose disclosure requirements as a way of ensuring symmetric information system in the capital market. Insider traders are prone to taking advantage of price-sensitive information in a way that creates a distortion in the market.

According to the IOSCO Financial Regulation Report (October 1998) *"The ideal securities market should be a free and open market with the prices thereon based upon the fullest possible knowledge of all relevant facts among traders. Any factor which tends to destroy or put in question this concept lessens the confidence of' the investing public in the marketplace and is therefore a matter of public concern."*

The harmful effects of insider trading are huge. However, because insider trading is often done on an exchange, through innocuous electronic means, it is easy to pass off as a victimless crime. In fact, the victims of insider trading are the unsuspecting consumers of the products in the first instance, and the rest of the law-abiding citizens who pick up the tab in lost revenue and less money to invest for the losing entity. It also increases the cost of capital for companies.

Under the common law, the law would only protect a victim of insider trading where a fiduciary relationship exists between the insider and the company, and such victim is oblivious of such relationship. Even then, the statutory sanctions against insider trading under the common law are criminal in the absence of civil remedies. See ***Regal (Hastings) Ltd v. Gulliver*** (1942) 1 All E.R. 378. The common law, in recognising the fiduciary duties owed by insiders of the company to the company itself, has failed to recognise the same for the shareholders of the company.

It is pertinent to note that efforts in tackling insider trading are market-wide. Self- Regulatory Organisations (SROs) such as NSE have also made provisions aimed at curbing the problem. Rule 17.2 of the NSE Rulebook imposes a duty on every Issuer to keep investors and the public fully informed of all factors, which might affect their interests. Particularly, issuers must make immediate disclosure of any information concerning their interests, which might reasonably have material effect on market activity in, and the prices or value of, listed securities. Similarly, every Issuer has an obligation to disclose on immediate basis, all information on material circumstances likely to affect its financial condition.

Furthermore, in May 2014 NSE established a "Close Period" during which principal officers and connected persons are denied the ability to trade in the issuer's securities. This is usually the one-month period preceding the release of a company's quarterly results, and the two-month period before the release of its annual results.

The Rules describe the Closed Period as the time where any of the following occurs:

a. declaration of financial results (quarterly, half-yearly and annual);
b. declaration of dividends (interim and final)
c. issue of securities by way of public offer or bonus, etc;
d. any major expansion plans or winning of bid or execution of new projects;
e. amalgamation, mergers, takeovers and buy-backs;
f. disposal of the whole or a substantial part of the undertaking;
g. any change in policies, plans or operations of the company that is likely to materially affect the prices of the securities of the company;
h. disruption of operations due to natural calamities;
i. litigation/dispute with a material impact; or
j. any information which, if disclosed, in the opinion of the person disclosing the same is likely to materially affect the prices of the securities of the Company.

The basis of compensation to such victim or its agents shall be the difference between the prices of the securities at the ordinary transaction and the insider dealing-related transaction. SEC is empowered under its Rule 601 to determine the quantum of compensation for insider dealing cases.

On its part, NSE may suspend trading in an instrument with effect from such time as it may determine if there are reasonable grounds to suspect the Issuer failed to comply with disclosure rules, as stipulated under NSE Rulebook. NSE may further impose such conditions on the procedure for lifting the suspension, as it considers appropriate.

Given that a phenomenal amount of investment could be lost in a single insider trading event, the need for a more elaborate public education on insider trading cannot be more glaring; so too is the need for a more robust policing of the markets.

It is pertinent for every listed company to note that the Closed Period shall be effective from fifteen (15) days prior to the date of any proposed meeting of the Board of Directors to consider any of the matters referred to above. The period also includes the date of circulation of the agenda papers pertaining to any of the matters referred to above, whichever is earlier, and up to twenty-four (24) hours after the price sensitive information is submitted to NSE.

Liability for Insider Trading

Liability for insider trading is both criminal and civil. Section 115 of ISA provides that any person who engages in insider dealing commits an offence punishable with a fine in a sum not less than N500,000.00 (in the case of a person not being a body corporate). In the alternative, the fine could be a sum equivalent to double the amount of profit derived by him or loss averted by the use of the information obtained in contravention of any of the provisions ISA. There is also an imprisonment for a term not exceeding seven years in the case of an individual.

Civil penalties include compensation from the insider trader pursuant to Section 116 (1) ISA. This provision empowers SEC or the Investments and Securities Tribunal (IST) to order an insider dealer or trader to compensate the victim in a transaction for the purchase or sale of securities.

Conclusion

Despite the detailed insider trading prohibitions in the Nigerian securities laws, it is quite underwhelming that there has not been any SEC prosecution for violations thus far. This lack of prosecution points to more endemic problems associated with the enforcement of the securities laws in Nigeria. Given that a phenomenal amount of investment could be lost in a single insider trading event, the need for a more elaborate public education on insider trading cannot be more glaring; so too is the need for a more robust policing of the markets.

Editor's Note

The NSE started 2019 on a sluggish note, shedding off significant points, with little hope of a speedy recovery. The Federal Government of Nigeria (FGN) recorded modest gains on the Ease of Doing Business index with measurable improvements in reduced processing time and documentation for company registration and immigration reforms. FGN scored low on developing the economy, hampered by low oil prices and poor infrastructure. The impending general elections in Nigeria come with elevated risk levels that significantly affect the economy before and after the elections. There is therefore an imminent danger of major policy somersaults, which may affect many investments.

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