

THE TAKEOVER PANEL

INSIDER DEALING

For some time past the Panel on Take-overs and Mergers and The Stock Exchange have been considering the problems of so-called insider dealing. They have come to the conclusion that such dealing, properly defined, should be made a criminal offence, enforcement being in accordance with normal Companies Acts practices. The Panel and The Stock Exchange have with the encouragement of the Governor of the Bank of England so advised the Department of Trade and Industry in connection with the Secretary of State's current review of possible amendments to Company Law. The Panel and The Stock Exchange believe that the mere enactment that insider dealing was an offence would be, as it has been in the United States, a very powerful deterrent.

The public announcement of this conclusion is not to be taken as involving any abdication by the Panel or The Stock Exchange of their general responsibilities or their surveillance over market transactions. In cases where insider dealing is suspected, however, both the Panel and The Stock Exchange are hampered not only by nominee trading but by the absence of any statutory power to interrogate or demand production of documents as well as by the fact that no statutory defence of qualified privilege yet exists to protect any possibly defamatory public statements they might make in connection with these matters. It is to be remembered also that the Panel only has jurisdiction over dealings occurring in the context of a take-over or merger. Insider dealing is by no means limited to this field. In this connection the Panel and The Stock Exchange consider it right to add that in their view the extent of so-called insider dealing has been much exaggerated. Some of the alleged insider dealing on the stock market results from newspaper tips, shrewd guesswork, careful assessment by financial analysts, special reports by brokers on particular companies and not least the view of the buyer or seller himself as to whether a company is likely to do badly or, on the contrary, to improve its profit performance or increase its dividend, or is a possible object of a take-over bid. Even when insider dealing is involved, the purchaser or seller, as the case may be, is less likely to be himself a director or employee of the company involved than a third party who has received information from some insider seeking either to

demonstrate his own importance or misguidedly to benefit a friend or, again, out of sheer careless talk.

Nonetheless, it remains the fact that insider dealing does take place although it is impossible to measure its precise extent. The Panel and The Stock Exchange consider that insider dealing is wholly reprehensible and that the time has now come when legislative measures should be taken to stop it.

The use of civil remedies alone has been fully canvassed in the Justice Report on this matter and in the one published by the City of London Solicitors' Company. Civil proceedings are likely to be expensive, time consuming and in themselves an insufficient deterrent. The Panel and The Stock Exchange agree with the conclusion of these Reports and consider that in the circumstances of this country the mischief cannot satisfactorily be dealt with without a criminal sanction. If there is to be a criminal sanction several considerations appear to follow.

Definition of Criminal Offence

The class of persons brought within the criminal sanction must be defined so as to restrict it to people who have a guilty mind. Broadly, an insider could be defined as any person who because of his employment or any confidential relationship with a public company is in possession of particular information about that company not known to the ordinary stockholders of the company concerned and which if known would be likely substantially to affect the market price of such company's securities. Such a person would commit an offence if in reliance upon such information he either bought or sold the shares of the company concerned or conveyed the said information to any third party in breach of confidence and with the intention that the third party should make a profit therefrom. The exact definition must of course be a matter for the Government and the Parliamentary draftsmen: several detailed definitions have, however, been considered and one of these appears in an Appendix to this statement. The Panel and The Stock Exchange do not, however, necessarily endorse this definition in every particular nor do they think it appropriate to lay down any final definition here. They merely indicate elements which ought to be covered in regard to legal sanctions.

Other Proposals

There remains the problem of establishing that insider dealing however defined has in fact taken place which has proved a stumbling block to the exercise of the Panel's own jurisdiction in the matter. In order to enable statutory sanctions to be enforced with certainty and expedition, it appears to the Panel and The Stock Exchange that modifications should be made in the existing law in three respects so that offences may be more readily discovered. These changes would also have a deterrent effect in discouraging insider dealing.

Nominee Holdings The existence of nominee companies and the possibilities of conducting business in nominee names is well established and has proved a matter of great convenience. It is not suggested that there should be any alteration in the existing practice. In the case with which the Panel and The Stock Exchange are here concerned, however, it may be essential quickly to go behind the nominee name in order to ascertain that of the beneficial owner. The Department of Trade and Industry already possesses in certain cases a power to obtain this information. If as is suggested the Police (rather than the Department of Trade and Industry) are to be the prosecuting authority, it might be more expeditious and convenient for a similar power to be given to them to obtain information as to the true beneficial ownership on the authority of a Chief Officer of Police.

Declarations as to dealings The existing requirement of notice to the company of any dealing by a director in the shares of the company and its registration in a book open to inspection at the company's office should be amended to require notice within 24 hours of any dealings by a director or officer (including auditor) of a company and the prompt registration of such dealings not only in the company's office but also in a public register to be maintained under the heading of each public company concerned at some convenient location such as the Companies Registration Office, City Road, London.

Information as to transactions The Panel has from time to time been frustrated in its enquiries by the refusal of a potential witness to disclose information about the matter under enquiry. It is considered essential that powers to require information should be given to the appropriate law enforcement body under the Companies Acts. The Department of Trade and Industry already possesses powers of enquiry in various matters concerning companies. No new principle would therefore be involved.

The Panel and The Stock Exchange believe, however, that the new provisions, which they suggest should be introduced into the criminal law, should be enforced in the same manner as other criminal offences under the Companies Acts—that is to say by the Police authority which in London would often mean the Fraud Squad. The present system of enquiry by the Department of Trade and Industry would be inappropriate in such cases, for it involves a procedure which is almost inevitably slow, not only for the reason that outside Inspectors who can only give part of their time to the matter are appointed but also because after the completion of the enquiry, if a prima facie case appears to be disclosed, much and often the whole of the matter is re-investigated by the Police, whose task it is to decide whether or not to prosecute. At least two recent cases have illustrated notoriously the delays which can arise. It might no doubt be possible to establish a special division of the Department of Trade and Industry with Power to enquire and

prosecute as in the case of the Inland Revenue but on general grounds it is thought preferable that this matter, like other company offences, should be left to the normal law enforcement authority, namely the Police.

2nd February, 1973.

APPENDIX

Definition

1. (a) Any person described in sub-paragraph (b) below who:
 - (i) is in possession of particular and confidential information about a public company (including information about a possible takeover bid for the shares of the company) which to his knowledge has not been made known to shareholders generally, by publication in the press or otherwise, and would if generally known be likely to have a substantial effect on the price at which the shares in that company are dealt in on any Stock Exchange; and
 - (ii) in reliance on such information engages in any transaction (whether by way of purchase, sale or otherwise) privately or through any Stock Exchange in respect of or involving shares in such company with the intention of securing an advantage for himself or for any other person; or
 - (iii) conveys such information to any other person with the intention that such person or any third party should enter into any such transaction as is mentioned in paragraph (ii) and that person or third party thereafter enters into such a transaction in reliance on such information,
shall be guilty of an offence.
- (b) The persons to whom this Section applies are:
 - (i) any person who at the time of the relevant transaction is, or at any time within the preceding 12 months was, a director, officer (including auditor), or employee of the company concerned or of any other company which is an interconnected body corporate with that company;
 - (ii) any person (including any banker, solicitor, accountant or stockbroker) has received in confidence any information on which he relies as aforesaid from any person who to his knowledge was at the time when such information was given a person falling within (i) above;
 - (iii) any person who by dishonest means has obtained such information upon which he relies as aforesaid.
2. Where information falling within 1. (a)(i) above relates to the possibility that the company concerned may make a take-over bid for or enter into a commercial transaction with another public company and such information might if generally known have a substantial effect on the

price at which the shares in that other company are dealt in on any Stock Exchange, Section 1.(a) shall apply in respect of any transaction in the shares of such other company.

3. Any court before whom a person is convicted of an offence under the foregoing Sections may, in addition to or substitution for any statutory penalty, order that such person shall either account to the company or companies whose shares are involved in any transaction giving rise to the conviction for any profit made by himself or by any other person by means of such transaction, or shall account to any person with whom he made the share transaction and may give directions as to the manner in which such account is to be taken and the amount certified upon the taking of such account to be due from any such person to any company or any other person shall be recoverable as a civil debt.

2nd February, 1973.