TOPIC 8: INSIDER TRADING

Lecture

- Insider information has the capacity to change financial position
- Insider trading will undermine the integrity of a company

  Insider: S1043A:
- An insider is a person who possesses "inside information" about financial products
- Who knows, or ought to reasonably know the information is "inside information" → material effect on share price if it is known
- *R v Rivkin*

  Inside information: S1042A:
- Information not generally available, and if it were available, a reasonable person would expect it to have a material effect on price/ value of particular security.
- This is not limited to directors' distributing information – anyone who has access to information and making it publicly available where it normally isn't

  R v Firns [19.275]

  Information not generally available: 1042C(1)(b)
- Information becomes generally available if
    - It has been made known in a manner that would bring it to the attention of investors
    - A reasonable period for it to be disseminated has elapsed

  Material effect on price
- Reasonable person would expect it to have a material effect on price – likely to influence investors in deciding whether to buy or sell financial products.
- Price sensitive information: *Hannes v DPP*

  Insider prohibitions
- Insider must not
    - S1043A(1)(d): Procure another person to buy/sell
    - S1043A(1)(c): buy/sell financial products
    - S1043A(2): communicate "inside information:

  Consequence
- Criminal offence

  Max penalty for a body corp. is approx. $8m or 3x profit made on inside information tip off
- Compensation
- Financial services civil penalty provision

UCL 19.235-245

  Insider trading
- Prohibited under Div 3 of Pt 7.10 of the CA
- Occurs where a person trades in shares while in possession of price-sensitive information not typically available
- Insider trading provisions cover a range of financial products
- Continuous disclosure provisions require disclosing entities to disclose price-sensitive information not typically available
- Timely information reduces opportunities for insider trading
- Three key theories as to why insider trading should be prohibited:

Fairness: market participants should have equal access to relevant information from company issuing securities
Fiduciary duty: person holding a position of trust should not make a personal profit from that position without consent of beneficiaries
Economic Efficiency: insider trading damaging to integrity of financial market
<u>Insider Trading Prohibitions</u>

- S1043A(1) contains primary prohibitions against insider trading
- (1)(c): insider must not apply for, acquire, or dispose of an agreement to apply for or dispose of relevant financial products
- (1)(d): An insider must not procure another person to apply for, acquire or dispose of, or to enter into an agreement to apply for, or acquire any relevant financial instruments
- S1043A(2): prohibits an insider communicating or tipping inside information to another person
- Prohibition only applies to financial products which can be traded on a financial market in Australia
- An insider must not, directly or indirectly, communicate information or cause the information to be communicated to another person if the insider knows, or ought to reasonably know the other person would likely
    - Apply for, acquire or dispose of, or enter into an agreement to apply for any tradable financial product
    - Procure a third person to apply for, acquire or dispose of, or enter into an agreement to apply for, acquire or dispose of any such tradeable financial securities

<u>Who is an insider?</u>

- Someone who possesses inside information (as per S1042A)
- An insider knows, or ought to reasonably know that the matters specified in the S1042A
- Insider knows, or ought to reasonably know that matters specified in s1042A definition of inside information are satisfied in relation to the information

R v Rivkin [2003]
FACT: McGowan was the CEO and major shareholder of Impulse Airlines
During 2000 and 2001, Impulse Airlines entered into a price war with Qantas, having an adverse effect on both companies
As a result, Impulse suffered adverse losses, while Qantas' share price were significantly affected
McGowan concluded in April 2001 confidential negotiations to sell Impulse to Qantas following ACCC approval
McGowan tipped off Rivkin to not trade his Qantas shares. Hours later, Rivkin arranged for his family to acquire 50,000 Qantas shares at $2.78 per share.
Rivkin sold the shares days later for $2.85 each.
HELD: Rivkin was found to breach the predecessor of S1043A(1), sentenced to nine months periodic detention with a fine of $30,000.
It was held that Rivkin was an insider in relation to Qantas, possessing information not normally available to the public.
Had the information become publicly available, it would have had a material effect on the Qantas share price.