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**THEMES AND THEORIES OF THE INSIDER TREADING
PROVISIONS OF THE 2004 SECURITIES SERVICES ACT**

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I hereby declare that I have read and understood the regulations governing the submission of Master of Laws dissertations, including those relating to length and plagiarism, as contained in the rules of this University, and that this dissertation conforms to those regulations.

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THEMES AND THEORIES OF THE INSIDER TRADING PROVISIONS OF THE 2004 SECURITIES SERVICES ACT

CHAPTER 1: HISTORY AND OVERVIEW

1.1 INTRODUCTION

According to Blackman *et al*, 'insider trading' initially referred 'to the sale and purchase of a company's shares, debentures or other securities by persons connected or associated with the company (the 'insiders'), who are in possession of confidential, 'price-sensitive' information...gained as a result of that association and not available to (other) shareholders or to the general public.'¹ The practice of insider trading was first made illegal in South Africa with the introduction of s 233 of the Companies Act 61 of 1973. By the criminalising of insider trading, the conduct of an insider trader has been classified as a wrong against society.² At present, the relevant provisions of the Securities Services Act of 2004 regulate such practices.³ The Act has repealed the Insider Trading Act 135 of 1998, which had previously governed criminal and civil liability in terms of the offence. The insider trading provisions of the Act form part of corporate governance regulations, which are aimed at improving the efficiency of financial markets.⁴

¹ Blackman *et al*, *Commentary on the Companies Act* (2004) vol 1 Revision Service 1 at 5-375.

² Harry McVea 'Fashioning a System of Civil Penalties for Insider Dealing: Sections 61 & 62 of the Financial Services Act 1986' (1996) *Journal of Business Law* 344 at 350.

³ Act 36 of 2004.

⁴ G:enesis 'The impact of South Africa's insider trading regime: A report for the Financial Services Board' (2004) at 8, available at <http://www.fsb.co.za> [visited on: 03/08/2006].

This dissertation focuses on the significant transformation that South Africa's insider trading laws have gone through since this practice was first outlawed in 1973. It aims to tease out and discuss some of the core themes of the Act, and in doing so, note the various consistencies that exist between these themes and those of South Africa's previous insider trading laws. A similarly important aim will be to determine whether the Act represents a different emphasis in regard to what has previously constituted the 'wrong' of insider trading. In addition, the relevant flaws and inadequacies of the Act that appear to have resulted from the legislature's attempt to 'toughen' up on the previous provisions as well as certain evidential problems will be discussed.

It will be shown that, despite the fact that there has been a general trend to broaden the offences as well as certain key definitions, notably that of an 'insider', so that the link between the Act and the previous enactments is not as obvious as it used to be, it is submitted that this link has not completely broken down.

1.2 THE VALUE OF MARKET INFORMATION AND THE OBJECT OF AN INSIDER DEALER

'Inside information' is information regarding a company that, if it were to be made public, would change the company's share price.⁵ This is because the market will respond to the information by altering the market price of the shares.⁶ The announcement by a company of a particularly profitable year, for example, is information that is capable of having an impact on the share price of a company.⁷ This information is likely to increase the market value of the shares in the company, making them more expensive to buy as well as more profitable

⁵ G:enesis, *supra* note 4, at 10.

⁶ Brenda Hannigan *Insider Dealing* (1998) at 3.

⁷ Gil Brazier *Insider Dealing: Law and Regulation* (1996) at 3-04.

to sell.⁸ However, an announcement by a company of an imminent profits warning would normally cause the securities of that company to reduce in value, making them cheaper to buy but also less valuable to sell.⁹ Such price-sensitive information is therefore valuable, being the information that the market relies on to determine the price of a particular commodity.¹⁰

The objective of an insider dealer is therefore to deal in securities when he is in possession of price-sensitive information (information which may alter the price of the securities).¹¹ This will be done so on the basis of information which has not yet been made public and which therefore has not had an effect on the share price.¹² A person (such as a director or manager of the company) may use this information to buy securities at their current price before the information in question becomes public, causing the price to rise, or to sell securities at their current price before their value falls upon the publication of the information.¹³ An example of a simple case of insider trading would be that of a 'company director who is aware of a dramatic mineral find on company land and who then proceeds to buy as many shares as possible in the company before the information is made public.'¹⁴

1.3 INSIDER TRADING AT COMMON LAW

In terms of the common law, directors stand in a fiduciary relationship to their respective companies and are therefore under a duty not to 'use for their own purpose anything, including trade secrets and confidential information, entrusted

⁸ Brazier, *supra* note 7, at 3-04.

⁹ *Ibid.*

¹⁰ Hannigan, *supra* note 6, at 2.

¹¹ Brazier, *supra* note 7, at 3-12.

¹² Derek Botha 'Control of Insider Trading in South Africa: A Comparative Analysis' (1991) 3 *SA Merc LJ* 1 at 2.

¹³ Paul L. Davies (ed) *Gower's Principles of Modern Company Law* 6th ed (1997) at 443.

¹⁴ Hannigan, *supra* note 6, at 5.

to them for use on behalf of the company.¹⁵ The use of confidential information for their own purposes is a breach of this duty and renders them liable to account to their company for any profits they may have made.¹⁶ A director is therefore under a duty to disclose any confidential price-sensitive information to his or her company.¹⁷

The English case of *Percival v Wright*¹⁸ appears to have established the generally accepted rule that directors do not stand in a fiduciary relationship to their individual shareholders and that therefore are not under a fiduciary duty to disclose any inside information in their possession to their shareholders when dealing with them. The case involved was an action by shareholders (plaintiffs) to set aside a sale of shares in a takeover deal on the ground that the directors, as purchasers, ought to have informed them that they were engaged in pending negotiations for the sale of the company, which would have significantly raised the value of the shareholders' shares. Swinfen Eady J held that::

'It is urged that the directors hold a fiduciary position as trustees for the individual shareholders, and that, where negotiations for sale of the undertaking are on foot, they are in the position of trustees for sale ... It is contended that a shareholder knows that the directors are managing the business of the company in the ordinary course of management, and implicitly releases them from any obligation to disclose any information so acquired. That is to say, a director purchasing shares need not disclose a large casual profit, the discovery of a new vein, or the prospect of a good dividend in the immediate future, and similarly a director selling shares need not disclose losses, these being merely incidents in the ordinary course of management. But it is urged that, as soon as negotiations for the sale of the undertaking are on foot, the position is altered. Why? The true rule is that a shareholder is fixed with knowledge of all the directors' powers, and has no more reason to assume that they are not negotiating a sale of the undertaking than to assume that they are nor exercising any other power . . . I am therefore of opinion that the purchasing directors were under no obligation to disclose to their vendor

¹⁵ Blackman *et al*, supra note 1, at 5-379.

¹⁶ *Ibid.*

¹⁷ *Ibid.*

¹⁸ (1902) 2 Ch 421 at 425-27.

shareholders the negotiations which ultimately proved abortive. The contrary view would place directors in a most invidious position, as they could not buy or sell shares without disclosing negotiations, a premature disclosure of which might well be against the best interests of the company. I am of opinion that directors are not in that position.

There is no question of unfair dealing in this case. The directors did not approach the shareholders with a view of obtaining their shares. The shareholders approached the directors, and named the price at which they were desirous of selling. The plaintiff's case wholly fails, and must be dismissed with costs.¹⁹

Percival v Wright, however, has been criticised.²⁰ According to Blackman *et al*, it is generally accepted that *Percival* did indeed decide that a director does not normally stand in a fiduciary relationship to the company's shareholders but that 'it is taking the decision too far when it is said to be authority for the proposition that directors never stand in a fiduciary relationship to the shareholders.'²¹ Browne Wilkinson in *Re Chez Nico (Restaurants) Ltd*,²² for example, interpreted *Percival*, to mean that 'in general directors do not owe fiduciary duties to shareholders but owe them to the company' and that 'in certain special circumstances fiduciary duties, carrying with them a duty of disclosure, can arise which places directors in a fiduciary capacity vis-a-vis the shareholders.'²³ Such special circumstances were emphasised by Mahoney JA, in the case of *Glandon Pty Ltd v Strata Consolidated Pty Ltd*.²⁴ According to Mahoney JA, in situations of a management buyout, a director purchasing the shares of a shareholder is in a position of advantage over the shareholders, having having been gained as a result of 'insider knowledge' from their position in the company. In this situation, a director 'is in a position of advantage and that advantage is of a special kind'

¹⁹ *Percival v Wright* (1902) 2 Ch 421 at 425-27.

²⁰ Blackman *et al*, *supra* note 1, at 5-383.

²¹ *Ibid* at 5-384.

²² (1992) BCLC 192.

²³ *Re Chez Nico (Restaurants) Ltd* (1992) BCLC 192 at 208.

²⁴ (1993) 11 ACSR 543 CA(NSW).

which may in appropriate circumstances give rise to fiduciary obligations.²⁵ In *Allen v Hyatt*,²⁶ the Privy Council held directors of the company to have put themselves in a fiduciary relationship with the individual shareholders by 'acting for them on the same footing as they were acting for the company itself, that was, as *agents*.'²⁷ The Court of Appeal in the New Zealand case of *Coleman v Myers*,²⁸ went beyond *Allen*, ruling that in certain circumstances directors may place themselves in a fiduciary relationship without having even acted as agents for their shareholders. In this case the directors, a father and son, of a small family company, were held to be liable to the shareholders in a take-over bid as a result of the special relationship that existed between them. The directors were held to have stood in a fiduciary relationship to the shareholders as a result of the company being closely held and that participation in the company was premised upon a relationship of mutual confidence and trust.²⁹ According to Woodhouse J:

'...it is not the law that anybody holding the office of director of a limited liability company is for that reason alone released from what otherwise would be regarded as a fiduciary responsibility owed to those in the position of shareholders of the same company....But there is nothing in the decision to suggest that in the case of a director the fiduciary relationship can arise only in an agency situation. On the other hand, the mere status of company director should not produce that sort of responsibility to a shareholder and in my opinion it does not do so. The existence of such a relationship must depend, in my opinion, upon all the facts of the particular case.'³⁰

Percival must therefore be seen on its facts, in that it was rightly decided according to its own special circumstances, the directors having been passive in this instance. As it was the shareholders who approached the directors, naming the price at which they were willing to sell, it seems as though there was almost

²⁵ *Glandon Pty Ltd v Strata Consolidated Pty Ltd* (1993) 11 ACSR 543 CA(NSW) at 547.

²⁶ (1914) 30 TLR 444.

²⁷ *Ibid* at 445.

²⁸ (1977) 2 NZLR 225 CA(NZ).

²⁹ (1977) 2 NZLR 225 CA(NZ); Blackman *et al*, *supra* note 1, at 5-387.

³⁰ *Coleman v Myers* (1977) 2 NZLR 225 CA(NZ) at 323.

a lack of causation.

Lastly, according to Milner, a director in a face-to-face transaction involving the sale of shares between himself and a seller or buyer, would in most cases have been under a duty to disclose any inside information which he possesses.³¹ This stems from the contractual principle that, 'although at common law there is no general duty on contracting parties to volunteer information, there is a duty to disclose where a contract is characterised by the involuntary reliance of the one party on the other for information material to his decision.'³² The court in the case of *Pretorius v Natal South Sea Investment Trust Ltd*,³³ followed Milner's view by holding that the directors of a company were obliged to disclose materially adverse inside information to an investor who applied for shares in the company.³⁴ According to Jooste, however, a distinction has to be drawn in the *Pretorius* case between stock exchange transactions and face-to-face transactions, where a duty to disclose would only arise in the latter under the common law.³⁵

From the above, it can be seen that, despite *Percival*, it was possible for a director to have placed himself in a fiduciary relationship to the individual shareholders of the company. The common law was therefore a legal possibility to an investor based on insider dealing in face-to-face transactions.³⁶ However, as the common law is limited to these transactions, it offered little recourse to such a shareholder ('victim') in stock exchange transactions and is therefore inadequate.

³¹ MA Milner 'Fraudulent Non-disclosure' (1957) 74 SALJ 177 in Richard D. Jooste 'Insider Dealing in South Africa' (1990) 107 SALJ 588 at 602.

³² *Pretorius v Natal South Sea Investment Trust Ltd* 1965 (3) SA 410 (W) at 417 in Blackman *et al*, supra note 1, at 5-394.

³³ 1965 (3) SA 410 (W).

³⁴ *Pretorius v Natal South Sea Investment Trust Ltd* 1965 (3) SA 410 (W) at 417.

³⁵ Jooste, supra note 31, at 602.

³⁶ *Ibid.*

CHAPTER 2: THE EVOLUTION OF SOUTH AFRICA'S INSIDER TRADING LAWS

2.1 SECTION 70NOV OF THE COMPANIES ACT 46 OF 1926

In England, the initial approach favoured in 1945 by the Cohen Committee was to rely on disclosure requirements, which in particular required disclosure by directors of their interests in the shares of their companies.³⁷ The committee was of the opinion that it would be unreasonable for a director to act, not on his general knowledge, but on a particular piece of information known to him and not to the general body of shareholders at the time.³⁸ The disclosure requirements were therefore thought to be the best way to safeguard this situation.³⁹ In South Africa, the Millin Commission supported the views of the Cohen Committee.⁴⁰ Section 70*nov* of the Companies Act 46 of 1926,⁴¹ was therefore introduced on the bases of the Commission's recommendation.⁴² This was South Africa's first attempt to curb insider dealing,⁴³ in terms of which, every company was required to keep a register of shares and debentures held by directors.⁴⁴ Changes in such holdings had to be recorded together with the date and price or other consideration.⁴⁵

³⁷ *Report of the Committee on Company Law Amendment* Cmnd 6659 of 1945 paras 86-87 in Hannigan, *supra* note 6, at 16.

³⁸ *Report of the Committee on Company Law Amendment* Cmnd 6659 of 1945 paras 86-87 in Blackman *et al*, *supra* note 1, at 5-394-5.

³⁹ *Ibid.*

⁴⁰ Blackman *et al*, *supra* note 1, at 5-394-5.

⁴¹ Introduced by s 49 of the Companies Amendment Act 46 of 1952.

⁴² Blackman *et al*, *supra* note 1, at 5-394-5.

⁴³ *Ibid.*

⁴⁴ Section 70*nov*; Richard D. Jooste 'The Regulation of Insider Trading in South Africa – Another Attempt' (2000) 117 *SALJ* 284 at 284.

⁴⁵ *Ibid.*

2.1.2 INSIDER TRADING AS A 'WRONG' COMMITTED AGAINST THE COMPANY ITSELF

As discussed above, directors are in a position of trust, standing in a fiduciary relationship to their respective companies.⁴⁶ As a result of this fiduciary relationship, a director's non-disclosure and use of 'inside information' for his own purpose was thought to harm the company itself.⁴⁷ It is submitted that s 70*nov* was based on this fiduciary rationale, having emphasised insider trading to be a wrong done to the company itself, rendering the director liable to his company alone. The 'wrong' committed by the 'insider' (director) was the breach of the fiduciary duty he owed to his company not to use its confidential information for his own purposes.⁴⁸ Section 70*nov* therefore seems to be representative of the legislature having viewed the fiduciary relationship in which an insider stands to his company as the core concept of insider trading, emphasising non-disclosure of inside information as the 'wrong' of insider trading.

2.2 THE COMPANIES ACT 61 OF 1973

Section 70*nov* did not expressly prohibit insider trading and proved to be ineffective.⁴⁹ Therefore, on the recommendation of the Van Wyk de Vries Commission,⁵⁰ new provisions⁵¹ were introduced into the 1973 Act. Section 233 made insider trading a criminal offence in South Africa.⁵²

⁴⁶ Blackman *et al*, supra note 1, at 5-379.

⁴⁷ *Ibid.*

⁴⁸ *Ibid.*

⁴⁹ Jooste, supra note 44, at 284.

⁵⁰ *Main Report of the Commission of Enquiry into the Companies Act* (RP 45/1970) in Jooste, supra note 44, at 284.

⁵¹ Sections 244 and 229-233 of the 1973 Act.

⁵² Jooste, supra note 44, at 284.

In terms of s 233, 'Every director, past director, officer or person who has knowledge of any information concerning a transaction or proposed transaction of the company or of the affairs of the company which, if it became publicly known, may be expected materially to affect the price of the shares or debentures of the company and who deals in any way to his advantage, directly or indirectly, in such shares or debentures while such information has not been publicly announced on a stock exchange or in a newspaper or through the medium of radio or television, shall be guilty of an offence.'⁵³ The penalty for contravention of s 233 was a fine not exceeding R8 000 or imprisonment for a period not exceeding two years or both such fine and such imprisonment.⁵⁴

The provisions introduced in 1973 however, also proved inadequate and ineffective as a result of there having been no prosecutions for their contravention.⁵⁵ In practice successful prosecution would have been unlikely due to the fact that s 233 merely contained a criminal sanction, requiring guilt to be proven beyond a reasonable doubt.⁵⁶ According to Botha, s 233's inability to prosecute was also due to its defective definition of insider-trading activities.⁵⁷ In addition, Bhana, having argued that the 'inadequacies in the legislation may have encouraged insiders to proceed with these illegal transactions', indicated four important defects of this section.⁵⁸ The first deficiency was that s 233 did

⁵³ Section 232 obliged directors, past directors, officers and certain persons to lodge with a company within a specified period, written notice regarding changes in any material interest in their shareholding in the company concerned; s 230 required every public company to keep a register of the material interests of its directors and officers in any shares and debentures of the company and s 224 prohibited directors from dealing in options in respect of the listed shares or debentures of his company, or its subsidiary or holding company, or a subsidiary of its holding company. These supporting provisions, including those listed in note 51 above, as well as s 233 were repealed by s 6 of the Companies Amendment Act No. 78 of 1989.

⁵⁴ Section 441 of the 1973 Act.

⁵⁵ Richard D. Jooste 'Insider Trading: A New Clampdown' (1991) 20 *Businessman's Law* 248 at 248.

⁵⁶ Russell Loubser 'Insider Trading and other Market Abuses (including the effective management of price-sensitive information)' (2006) at 5-6, available at: <http://www.jse.co.za/informational/insider/trading.pdf> [visited on: 01/08/2006].

⁵⁷ Botha, supra note 12, at 17.

⁵⁸ Bhana, N 'Take-over Announcements and Insider Trading Activity on the Johannesburg Stock Exchange' (1987) 18(4) *South African Journal of Business Management* 198 at 201 in Botha, supra note 12, at fn 15.

not encompass the activities of secondary insider traders ('tippees') who traded for their own benefit and account.⁵⁹ Secondly, it did not prohibit insider dealing by the directors and officers of an acquiring company in the shares of the target company.⁶⁰ Thirdly, directors and officers of an acquired company were not prohibited from dealing in shares in their own company prior to the announcement of a takeover deal.⁶¹ Fourthly, no provision was made for the lapse of a reasonable period after the public announcement of information.⁶² As will be discussed in more detail below, the fact that s 233 only included a very narrow range of persons within its prohibition was one of the more serious factors for there having been no prosecutions. The provisions introduced by the 1973 Act were therefore repealed by the Companies Amendment Act 78 of 1989 ('the 1989 Act').⁶³

2.2.1 INSIDER TRADING AS A 'WRONG' COMMITTED AGAINST THOSE WHO DEAL WITH INSIDERS

It is submitted that the enactment of s 233 is indicative of a fundamental shift in the law's attitude as to what had constituted the 'wrong' of insider trading. This change resulted from the Van Wyk de Vries Commission having reached the conclusion that insider trading did not cause harm to the company itself but that it could cause loss to those who deal with insiders.⁶⁴ It was further thought, that if some form of control was to be introduced, it should not be done in the area of the relationship between the director and his company.⁶⁵ This is a departure from the legislative approach taken in regard to s 70*nov*, which merely rendered

⁵⁹ Botha, *supra* note 12, at fn 15.

⁶⁰ *Ibid.*

⁶¹ *Ibid.*

⁶² *Ibid.*

⁶³ *Ibid* at 1.

⁶⁴ *Main Report of the Commission of Enquiry into the Companies Act* (RP 45/1970), para 44.50 in Blackman *et al*, *supra* note 1, at 5-375.

⁶⁵ *Main Report of the Commission of Enquiry into the Companies Act* (RP 45/1970), para 44.50 in Blackman *et al*, *supra* note 1, at 5-394-6.

an insider's conduct wrongful in relation to his company. This is evidenced by the fact that an 'insider' in contravention of s 233, was criminally liable as a result of the harm done to those persons with whom the insider traded.

2.3 THE 1989 AMENDMENT ACT AND THE 1990 SECOND AMENDMENT ACT

The provisions that were introduced in 1973 were repealed by the 1989 Act. Section 440F was introduced as the new anti-insider trading provision.⁶⁶ Section 440F(1) contained a general anti-fraud provision, having been based on the United States Rule 10b-5 of the Securities and Exchange Act of 1934.⁶⁷ However, s 440F was thought to be inappropriate as a result of its questionable draftsmanship and conceptual difficulties and was therefore never put into force.⁶⁸ Section 440F⁶⁹ was therefore repealed by the Companies Second Amendment Act 69 of 1990 ('the 1990 Act') and substituted by a new s 440F.⁷⁰ Both the 1989 Act and the 1990 Act were introduced 'in an obvious attempt to boost investor confidence in the securities market' to provide for 'new measures to combat the perceived anathema of insider trading.'⁷¹

The new s 440F(1) made it an offence for any person (directly or indirectly) to knowingly deal in a security on the basis of unpublished price-sensitive information in respect of that security, if that person knew 'that such information

⁶⁶ Section 440F was to be inserted into the Companies Act by s 4(b) of the Companies Amendment Act 78 of 1989; Stephanie M Luiz 'Insider Trading Regulation – If at First You Don't Succeed...' (1999) 11 *SA Merc LJ* 136 at 136.

⁶⁷ *Ibid.*

⁶⁸ Richard D. Jooste 'Insider Dealing in South Africa – The Criminal Aspects' (1990) 4(1) *De Ratione* 21 in Botha, *supra* note 12, at 9.

⁶⁹ As introduced by the 1989 Act.

⁷⁰ Section 3 of the 1990 Act. This dissertation is only concerned with the provisions that have been put into force in South Africa and therefore s 440F (as substituted by the 1989 Amendment Act) will not be discussed any further. All future references to s 440F are references to the new s 440F as substituted by the 1990 Amendment Act.

⁷¹ Jooste, *supra* note 44, at 248.

has been obtained - (a) by virtue of a relationship of trust or any other contractual relationship, whether or not the person concerned is a party to that relationship; or (b) through espionage, theft, bribery, fraud, misrepresentation or any other wrongful method, irrespective of the nature thereof.’ The penalty for contravention of section 440F was increased to a fine not exceeding R500 000, imprisonment for a period not exceeding 10 years or to both the fine and the period of imprisonment.⁷² Section 440F defined the concept of ‘unpublished price-sensitive information’⁷³ and in addition, in order to assist the prosecution in proving the offence,⁷⁴ included certain rebuttable presumptions⁷⁵. It is also important to note that s 440F(4)⁷⁶ represented a significant extension of liability from that of s 233, as it for the first time expressly provided for a civil remedy, which was available to any person who had suffered loss or damage as a result of the contravention of its provisions. Section 440G, which was introduced by the 1989 Act and amended by the 1990 Act, imposed an obligation on certain

⁷² Section 441(1)(a) which was inserted by s 3 of the 1990 Second Amendment Act.

⁷³ Section 440F(2) provided: ‘For the purposes of this section –

(a) “unpublished price-sensitive information”, in respect of a security, means information which –
 (i) relates to matters in respect of the internal affairs of a company or its operations, assets, earning power or involvement as offerer or offeree company in an affected transaction or proposed affected transaction;

(ii) is not generally available to the reasonable investor in the relevant markets for that security; and

(iii) would reasonably be expected to affect materially the price of such security if it were generally available;

(b) ‘generally available’ means available in the sense that such steps have been taken, and such time has elapsed, that it can be reasonably expected that such information as referred to in paragraph (a) is or should be known to such investor as referred to in subparagraph (ii) of paragraph (a).’

⁷⁴ Botha, *supra* note 12, at 13.

⁷⁵ Section 440F(3) provided the following: ‘If at criminal proceedings at which an accused is charged with an offence under subsection (1), it is proved that –

(a) the accused was in possession of unpublished price-sensitive information in respect of the security in question at the time of the alleged commission of the offence; or

(b) unpublished price-sensitive information was obtained in the manner contemplated in subsection (1)(a) or (b), he or it shall be deemed, unless the contrary is proved, in the case of –

(i) paragraph (a), to have knowingly dealt in that security on the basis of such information;

(ii) paragraph (b), to have known that such information was so obtained.’

⁷⁶ Section 440F(4) of the 1973 Act (as inserted by the 1990 Act) provided: ‘(a) Any person who contravenes subsection (1) shall be liable to any other person for any loss or damage suffered by that person as a result of such contravention.

(b) In the case of dealings in a security on a stock exchange or a financial market as defined in section 1 of the Financial Markets Control Act, 1989 (Act No. 55 of 1989), the plaintiff shall not need to prove intention or negligence towards him or it in an action contemplated in paragraph (a).’

owners of listed securities to furnish certain information to the Securities Regulation Panel (the 'SRP')⁷⁷ and to the stock exchange.⁷⁸ However, despite being potentially broad in their application, these provisions were also repealed, as there were no prosecutions for their contravention.⁷⁹

2.4 THE INSIDER TRADING ACT NO. 135 OF 1998 AND THE SECURITIES SERVICES ACT 36 OF 2004

In January 1999, new provisions governing both criminal and civil liability for insider trading were introduced by the Insider Trading Act 135 of 1998 ('the Insider Trading Act').⁸⁰ One of the motivations behind the enactment of the Insider Trading Act was South Africa's re-integration into the international financial markets and the Government's desire to create an environment conducive to foreign investment.⁸¹ These motivations were based on the assumption that 'investors would flee from a financial market in which insider trading is perceived to be rife and in which strong statutory and regulatory

⁷⁷ The SRP was established in terms of 440B (inserted by s 4(b) of the 1989 Act) and was given the function to of supervising dealings in securities (s 440C(1)(b)). It was further given the power to summon people to appear before it to be interrogated and to produce documents that may assist it in its investigations (s 440D).

⁷⁸ Section 440G(1) provided: 'The panel may require panel by notice in the *Gazette* that every person who is or becomes directly or indirectly the beneficial owner of more than 10 per cent, or such other percentage as may be prescribed by the panel by notice in the *Gazette*, of any class of equity security (other than a security exempted in terms of rules) which is dealt on a stock exchange, or who is a director or an officer of the issuer of such security, lodge, at the time of the listing of such security on a stock exchange, or within 10 days after he or it becomes such beneficial owner, director or officer, a statement with the panel of the amount of all equity securities of such issuer of which he or it is the beneficial owner, and within 10 days after the close of each calendar month thereafter, if there has been any change, in such manner as may be determined by the panel by notice in the *Gazette*, in such ownership during such month, file with the panel a statement indicating such change in his or its ownership as has occurred during the calendar month.' Failure to comply with the disclosure requirements was a criminal offence, carrying a penalty of a maximum fine of R20 000, imprisonment for a period of up to five years or both (s 440G(2) read with s 441(1)(c)).

⁷⁹ Luiz, *supra* note 66, at 137. Section 17 of the Insider Trading Act repealed s 440F.

⁸⁰ The Insider Trading Act was assented to on 20 November 1998 and came into effect on 17 January 1999 (see Proc 2 in *Government Gazette* 19666 of 15 January 1999).

⁸¹ *Final Report of the King Task Group into Insider Trading Legislation* (21 October 1997) at para 1.2 in Jooste, *supra* note 44, at 285.

measures for combating the practice are absent.⁸²

Since 2004, however, the market abuse of insider trading has fallen under the Securities Services Act 36 of 2004 ('the Act').⁸³ The Act was similarly enacted in order to increase investor confidence in the South African financial markets by contributing *inter alia*, to the maintenance of a stable financial market environment.⁸⁴ The common motivation behind the enactment of s 440F, the Insider Trading Act and the Act, has therefore been the attempt of improving the attractiveness and efficiency of South Africa's financial markets. As will be discussed, this motivation is based on the notion that insider trading decreases investor confidence in the market by creating an unfair playing field, making it harder for companies to attract funds.

As will be discussed, the Insider Trading Act considerably broadens the range of offences relating to insider trading.⁸⁵ It did this by providing for three offences, namely: 'dealing on one's own account'; 'dealing on someone else's behalf'; 'encouraging' or 'discouraging' dealing; and 'improper disclosure' of inside information.⁸⁶ In addition, certain defences to the offences were provided, where liability could be imposed if the offender failed to prove one of the related defences.⁸⁷ The definitions of an 'insider' and 'inside information' were similarly widely defined and a civil remedy was provided as a mechanism for people who have been 'affected' by insider trading. The penalty for insider dealing under the Insider Trading Act was a fine not exceeding R2 million, or to imprisonment for a

⁸² Patrick C. Osode 'The new South African Insider Trading Act: Sound law reform or legislative overkill?' (2002) 45 *Journal of African Law* 239 at 240.

⁸³ See Chap VIII of the Act. The Insider Trading Act was repealed by s 117 of the Act.

⁸⁴ The central aims of the Act are stated in s 2, being to '(a) increase confidence in the South African financial markets by- (i) requiring that securities services be provided in a fair, efficient and transparent manner; and (ii) contributing to the maintenance of a stable financial market environment; (b) promote the protection of regulated persons and clients; (c) reduce systemic risk; and (d) promote the international competitiveness of securities services in the Republic.'

⁸⁵ Luiz, *supra* note 66, at 138.

⁸⁶ Sections 2(1)(a); 2(1)(b) and 2(2) of the Insider Trading Act.

⁸⁷ Sections 4(1) and (2) of the Insider Trading Act.

period not exceeding ten years, or to both such a fine and such imprisonment.⁸⁸

As a brief introduction, it should also be noted that the new provisions are similar but not identical to those of the former Insider Trading Act, having been introduced in an attempt to improve on the latter.⁸⁹ The Act prohibits the same forms of conduct as did its predecessor and similarly provides for both criminal and civil liability.⁹⁰ The current definition of 'inside information' is almost identical to the previous, however the penalty for insider trading has dramatically increased to a fine not exceeding a staggering R50 million or imprisonment for a period not exceeding ten years or both such fine and imprisonment.⁹¹

2.4.1 THE MODERN JUSTIFICATION FOR THE STATUTORY REGULATION OF INSIDER TRADING

According to Blackman *et al*, it is 'now generally accepted that the reason for prohibiting insider trading is the inherent unfairness of the practice, with the consequent corrosive effect that it has on confidence in the market in shares.'⁹² Both the market fairness and market efficiency rationales for the regulation of insider trading are intimately connected,⁹³ their focus being on the market impact of using inside information.⁹⁴ This must be seen in contrast to the fiduciary rationale discussed above, where the focus was on the misuse of information by persons having some fiduciary or similar relationship with the

⁸⁸ Section 5 of the Insider Trading Act.

⁸⁹ Richard D. Jooste 'A Critique of the Insider Trading Provisions of the 2004 Securities Services Act' (2006) 3 *SALJ* 437 at 437.

⁹⁰ However, it must be noted that the provisions of the Act and the Insider Trading Act are not identical.

⁹¹ Section 115(a) of the Act.

⁹² Blackman *et al*, *supra* note 1, at 5-378.

⁹³ *Ibid.*

⁹⁴ Ministry of Economic Development, Manatu Ohanga 'Part 1: Policy Justifications for the Regulation of Insider Trading' (May 2002) *Fundamental Review*, available at: http://www.med.govt.nz/templates/MultipageDocumentPage_4220.aspx [visited: 20/11/2007].

issuer of securities.⁹⁵

In terms of the fairness argument, it is argued that fairness 'requires equality of opportunity and that the inherent unfairness of the practice' of insider trading is the reason for prohibiting it.⁹⁶ It is argued that all investors should have an equal opportunity to obtain and evaluate information relevant to their trading decisions,⁹⁷ where an 'insider is not placed, for reasons that have no merit, in a better position than outsiders either to make gains or avoid losses in securities transactions.'⁹⁸ The market fairness theory therefore aims at preventing an insider from trading on the basis of information obtained from a non-public source, since that information places the insider an informational advantage over other investors.⁹⁹

In terms of the efficient capital market hypothesis, 'all available information about a company's financial future is instantly and fully reflected in its share price.'¹⁰⁰ It is said that a market participant in an informationally efficient market can be confident that share prices accurately reflect a company's prospects, which will in turn ensure the efficient allocation of capital resources in that market.¹⁰¹ In terms of the market efficiency rationale, insider traders are thought to undermine the integrity of the market, rendering it inefficient.¹⁰² An insider trader is said to harm the efficiency of the market by dealing in "shares when in possession of 'price-sensitive' information which has not been made public and which therefore has not

⁹⁵ Ministry of Economic Development, Manatu Ohanga, *supra* note 94.

⁹⁶ *Ibid.*

⁹⁷ *Ibid.*

⁹⁸ French and Rider 'Should Insider Trading be Regulated? Some Initial Considerations' (1978) 95 *SALJ* 79 at 81.

⁹⁹ Ministry of Economic Development, Manatu Ohanga, *supra* note 94.

¹⁰⁰ Botha, *supra* note 12, at 2.

¹⁰¹ *Ibid.*

¹⁰² Blackman *et al*, *supra* note 1, at 5-378.

had an effect on the share price.”¹⁰³ Such practices are said to decrease investor confidence in the market by creating an unfair playing field, making it harder for companies to attract funds.¹⁰⁴ It is thought that if people fear that insiders will regularly profit at their expense, they will not nearly be as willing to invest.¹⁰⁵ By undermining the public confidence in the financial market, the perceived harm of insider trading is to the integrity of the market itself (the protection of the financial market as a whole) rather than particular persons.¹⁰⁶

The aim of modern insider trading legislation is therefore to discourage persons from taking unfair informational advantages and to punish those who fail to comply.¹⁰⁷ It is hoped to preserve (as far as possible) a ‘level playing field’, in terms of which information is promptly made public through disclosure to the public and insiders are deterred from abusing their position.¹⁰⁸ This would allow all investors to deal on the market on a more or less equal footing as everyone would have access to material information.¹⁰⁹

¹⁰³ Botha, *supra* note 12, at 2.

¹⁰⁴ G:enesis, *supra* note 4, at 10.

¹⁰⁵ David D Haddock ‘*Insider Trading*’, available at: <http://www.econlib.org/library/ENC/Insidertrading.html> [visited:03/08/2006].

¹⁰⁶ Blackman *et al*, *supra* note 1, at 5-378.

¹⁰⁷ Brazier, *supra* note 7, at 3-16.

¹⁰⁸ *Ibid* at 3-15.

¹⁰⁹ *Ibid*.

CHAPTER 3: 'INSIDER'

3.1 PRIMARY AND SECONDARY INSIDER DEALING

There are two groups of 'insider', namely primary and secondary insiders. Primary insider trading is dealing by an 'insider'.¹¹⁰ Secondary insider trading is dealing by a person whose source of information is an 'insider'.¹¹¹ Another term for a secondary insider trader is a 'tippee'.¹¹² It is thought that 'tippees' should also be prevented from being well-informed if a level playing field is to be preserved.¹¹³ A common element of the offences under the Act, as was the case with the Insider Trading Act, is that the accused must be an 'insider' in order to be held either criminally or civilly liable. This was also a requirement under s 233¹¹⁴ and s 440F, despite the fact that neither section provided an explicit definition of 'insider'.

3.2 AN 'INSIDER' IN TERMS OF S 233 OF THE 1973 ACT

Previously, the legislature, when drafting s 233, failed to provide an explicit definition of the concept of an 'insider'.¹¹⁵ It was clear, however, that the only persons who were capable of committing the offence were directors, past directors, employees and persons in accordance with whose directions or instructions any of the directors of a company were accustomed to act.¹¹⁶ These people are considered to come into possession of unpublished price-

¹¹⁰ Jooste, *supra* note 44, at fn 16.

¹¹¹ *Ibid.*

¹¹² *Ibid.*

¹¹³ Brazier, *supra* note 7, at 3-14.

¹¹⁴ It must be noted, as previously mentioned, that there was no civil liability under s 233.

¹¹⁵ Botha, *supra* note 12, at 6.

¹¹⁶ Section 233 and the definition of 'person' in s 229 of the 1973 Act. Section 299 also defined an officer as 'any employee who would be in possession of any information consequent upon his immediate relationship with the directors of the company immediately before a public announcement is to be made under section 233.'

sensitive information, as a result of their close connection or relationship with the relevant company.¹¹⁷ The application of s 233 was therefore restricted to the most usual category of insiders, having merely captured primary insiders within its prohibition.¹¹⁸ However, these provisions have been said not to have captured the category of primary insiders in its entirety.¹¹⁹ This is due to the fact that an individual who was not a director or past director, or who did not fall within the relevant definitions of an officer or person but who had obtained the inside information by virtue of a relationship of trust or any other contractual relationship, did not fall within the ambit of s 233.¹²⁰

3.3 AN 'INSIDER' IN TERMS OF S 440F(1) OF THE 1973 ACT (AS INSERTED BY THE 1990 ACT)

Section 440F extended liability for the crime of insider trading by including both primary and secondary insider dealing within its prohibition.¹²¹ Section 440F ensnared three categories of wrongdoers; the first category was that of the primary insider,¹²² who by virtue of a relationship of trust or any other contractual relationship had access to inside information.¹²³ According to Jooste, this category was not restricted to fiduciary relationships but also included those, which fell short of fiduciary relationships but in which there was an expectation of confidentiality between the parties.¹²⁴ The second category was that of the 'tippee', who had obtained the information from 'the 'primary insider' or from

¹¹⁷ Brazier, *supra* note 7, at 3-13.

¹¹⁸ Botha, *supra* note 12, fn 15.

¹¹⁹ Jooste, *supra* note 31, at 596.

¹²⁰ *Ibid.*

¹²¹ *Ibid.* Section 440F(1) made it an offence for any person (directly or indirectly) to knowingly deal in a security on the basis of unpublished price-sensitive information in respect of that security, if that person knew 'that such information has been obtained - (a) by virtue of a relationship of trust or any other contractual relationship, whether or not the person concerned is a party to that relationship; or (b) through espionage, theft, bribery, fraud, misrepresentation or any other wrongful method, irrespective of the nature thereof.'

¹²² Jooste, *supra* note 31, at 596.

¹²³ Section 440F(1).

¹²⁴ Jooste, *supra* note 31, at 596.

another ‘tippee’,¹²⁵ the information being passed on to the ‘tippee’ either voluntarily (without duress) or inadvertently’.¹²⁶ This category covered secondary insider trading, being dealing by a person (an outsider) whose source of information was a primary insider.¹²⁷ The third category included any person, whether insider or outsider, who gained access to the inside information through espionage, theft, bribery, fraud, misrepresentation or any other wrongful method.¹²⁸

3.4 THE DEFINITION OF ‘INSIDER’ IN TERMS OF S 72 OF THE ACT (S1(VIII) OF THE INSIDER TRADING ACT)

In terms of s 72 of the Act, an ‘insider’ has been defined to mean ‘a person who has inside information – (a) through – (i) being a director, employee or shareholder of an issuer of securities listed in a regulated market to which the inside information relates; or (ii) having access to such information by virtue of employment, office or profession; or (b) where such person knows that the direct or indirect source of the information was a person contemplated in paragraph (a)’. The definition of ‘insider’, as provided for in terms of s 72, is almost identical to that of s 1(VIII) of the previous Insider Trading Act, the only difference being the fact that the latter referred to an ‘individual who has inside information’ as opposed to a ‘person who has inside information’.¹²⁹

Primary insider trading: persons having access to inside information ‘through being’ a director, employee or shareholder

¹²⁵ Jooste, supra note 31, at 596.

¹²⁶ Section 440F(1).

¹²⁷ Jooste, supra note 44, at 286.

¹²⁸ Section 440F(1); Jooste, supra note 31, at 596.

¹²⁹ Any reference to the current definition of ‘insider’ is therefore intended to cover that of both s 72 of the Act and s 1(viii) of the Insider Trading Act, both being virtually identical.

The first category of primary 'insider' under s 72(a)(i) of the Act (s 1(viii)(a)(i)¹³⁰ of the Insider Trading Act) is that of a person who has 'inside information' through 'being a director, employee or shareholder of an issuer of securities listed in a regulated market to which the inside information relates'.¹³¹ Gower, commenting on the UK legislation, which is almost identical to ours, is of the opinion that 'the "through being" test is simply a "but for" test'.¹³² A junior employee who happened to see inside information in the non-public part of the employer's premises, for example, would fall within the category of insider.¹³³ This would be the case even if the duties of the employment did not involve acquisition of that information.¹³⁴ However, it is thought that if an employee came across the information in a social context, he would not fall within this category of insider, even if the information related to the worker's employer.¹³⁵ In order for the employee to become an 'insider' there must be a causal link between the employment and the acquisition of the information, 'but not in the sense that the information must be acquired in the course of the employee's employment'.¹³⁶

Primary insider trading: persons having access to inside information 'by virtue' of their position

Section 72 of the Act (s 1(viii)(a)(ii) of the Insider Trading Act)¹³⁷ provides for a second category of primary 'insider', which includes those persons who have access to inside information by virtue of their employment, office or profession. This would include those persons who, although not connected with a company,

¹³⁰ Section 1(viii) of the Insider Trading Act, defined an 'insider' to mean 'an individual who has inside information- (a) through- (i) being a director, employee or shareholder of an issuer of securities or financial instruments to which the inside information relates'.

¹³¹ Luiz, *supra* note 66, at 141.

¹³² Davies, *supra* note 13, at 465.

¹³³ *Ibid.*

¹³⁴ *Ibid.*

¹³⁵ *Ibid.*

¹³⁶ *Ibid.*

¹³⁷ Section 1(viii) of the Insider Trading Act defined an 'insider' to mean 'an individual who has inside information- (a) through- (ii) having access to such information by virtue of his or her employment, office or profession'.

may still have direct access to the inside information as a result of their position, for example: lawyers, bankers, auditors and public relations consultants.¹³⁸ The prosecution does not need to establish a direct connection or relationship between a person's employment, office or profession and the issuer of securities to which the inside information relates.¹³⁹ This is because the 'access by virtue' category of 'insider' as provided for in s 72(a)(ii)¹⁴⁰ does not mention an 'issuer of securities'.¹⁴¹

Secondary insider dealing: 'tippee' liability

The third category of 'insider' in terms of s 72 of the Act (s 1(viii)(b) of the Insider Trading Act)¹⁴² is that of the secondary insider or 'tippee'.¹⁴³ Again, it is not necessary to establish that the tippee's informant was connected with the relevant company.¹⁴⁴ The prosecution is only required to prove that the 'tippee' knew that the inside information came directly or indirectly from an inside source.¹⁴⁵ An inside source would include any director, employee or shareholder of a company as well those who had access to such information by virtue of their employment, office or profession.¹⁴⁶

'Person' as opposed to 'individual'

¹³⁸ Blackman *et al*, supra note 1, at 5-394-15.

¹³⁹ Luiz, supra note 66, at 141. Luiz is referring to the corresponding provision (s 1(viii)(a)(ii)) of the Insider Trading Act.

¹⁴⁰ Section 1(vii)(a)(ii) of the Insider Trading Act.

¹⁴¹ Blackman *et al*, supra note 1, at 5-394-15.

¹⁴² Section 1(viii) of the Insider Trading Act defined 'insider' to mean an individual who has inside information-

'(b) where such individual knows that the direct or indirect source of the information was a person contemplated in paragraph (a)'.

¹⁴³ Luiz, supra note 66, at 141.

¹⁴⁴ Jooste, supra note 44, at 289; Jooste is referring to the corresponding provision of s 1(viii)(b) of the Insider Trading Act.

¹⁴⁵ *Ibid.*

¹⁴⁶ Blackman *et al*, supra note 1, at 5-394-16.

A significant change that was re-introduced¹⁴⁷ by the Act is that the offences (and civil) wrongs can now be committed by a 'person'. As a result, it is not only natural persons who may fall foul of the Act but also juristic persons which would include corporate bodies, such as companies.¹⁴⁸ Previously, the offences under the Insider Trading Act could only have been committed by an 'individual', juristic persons having been excluded from its ambit.¹⁴⁹ In addition, partnerships and trusts have also expressly included within the Act's definition of 'person'.¹⁵⁰ The Act's definition of 'insider' is therefore wider in ambit than that of the Insider Trading Act, representing an extension of liability from what was previously provided.

It is not clear why the legislature thought it necessary to include these corporate entities within the ambit of liability of the Act. One possible reason could be the fact that 'they are now able to acquire their own shares and the shares in their holding companies.'¹⁵¹ It seems as though this extension of liability could be representative of the legislature's commitment to the policy objective of deterrence.¹⁵²

3.5 THE CURRENT DEFINITION OF 'INSIDER': AN ANALYSIS AND COMPARISON

From the previous discussion, it was shown that the inclusion of traditional insiders within the category of primary 'insider', besides being a theme of the Act itself, has also been a common theme of all South Africa's previous insider trading laws. Although the extent has varied in the different enactments, this

¹⁴⁷ This was also the position under s 440F(1), where the offence of insider dealing could also have been committed by 'any person'.

¹⁴⁸ Jooste, *supra* note 89, at 438.

¹⁴⁹ Luiz, *supra* note 66, at 143; Jooste, *supra* note 89, at 438.

¹⁵⁰ Section 72 of the Act.

¹⁵¹ Sections 85 and 89 of the Companies Act 61 of 1973; Jooste, *supra* note 89, at fn 16.

¹⁵² The policy objective of deterrence will be discussed in more detail on page 50.

basic category of 'primary insider' still requires that a person be 'connected' to the relevant issuer of securities.¹⁵³ As s 233 only included traditional insiders within its prohibition, its aims was not to target 'any individual' with inside information, but was rather restricted to those persons who were in charge of the information or who were directly connected with the company. By merely targeting persons, such as upper management, the legislature seemed to have been more concerned about the company, which is a very odd feature when one would think that any employee would have been covered.

The inclusion of a second category of primary 'insider', being those persons having access to inside information 'by virtue' of their position as well as secondary insiders ('tippees') has also been a common theme under s 440F(1), s 1(viii) of the Insider Trading Act and s 72 of the Act. As previously discussed, the modern rationale for the regulation of insider trading has meant that all trading on inside information is regulated, whether by true insiders or not. In this way it is not only traditional insiders who are regularly privy to such information who are barred from trading but also 'tippees' and persons who have gained access to inside information 'by virtue' of their position. In this respect, s 440F(1), was similar in effect to the current definition, however, by having required the inside information to have been obtained 'by virtue' of a relationship of trust or any other contractual relationship, it was also narrower in ambit than the current definition.¹⁵⁴ It is submitted that, unlike the Act, s 440F(1) expressly included the illegal acquirer within its ambit and was therefore also wider in ambit than the current definition.¹⁵⁵

The inclusion of 'by virtue' and secondary insiders seems to be break down the philosophy under s 233, in terms of which it is only senior management (those

¹⁵³ Blackman *et al*, supra note 1 at 5-378.

¹⁵⁴ *Ibid* at 5-394-15.

¹⁵⁵ The third category of 'insider' under s 440F(1) was that of any person 'who gained access to the inside information through espionage, theft, bribery, fraud, misrepresentation or any other wrongful method irrespective of the nature thereof.'

people actually in charge of the information) or people connected with the company who should be subject to the prohibition against insider trading. Therefore, an important theme of the Act is that it is not restricted to targeting only those persons in charge of the information or high up in the company nor does require a person to have come in possession of price sensitive information through his or her position in the company. This is in direct contrast to s 233 where only trading by insiders was made a criminal offence.

From the above it can be seen that there has been a trend in South Africa's insider trading laws to broaden the definition of 'insider' so as to include an extended range of persons within their respective prohibitions. As a result, the link between the Act and the previous enactments is not as obvious as it use to be. However, it is submitted, that although the Act has placed a greater on the possession of 'inside information', the link with s 233 has not been completely broken down. This is due to the fact in order to commit an offence under the Act, a person must still either have come into possession of 'inside information' as a primary 'insider' or he or she must have must known that the direct or indirect source of the information was a primary 'insider'.¹⁵⁶ As a result, there is still an impetus on how an 'insider' came into possession of the 'inside information', although to a lesser extent.

3.6 IS THE TRANSMISSION OF 'INSIDE INFORMATION' A NECESSARY REQUIREMENT UNDER S 72 (A)(II)?

Academics have expressed some concern as to exactly how far the 'by virtue' requirement under s 72(a)(ii) will reach.¹⁵⁷ The following example has been provided to illustrate this difficulty: if while taking their order, a barman at a local golf club overhears a conversation involving 'inside information' being discussed

¹⁵⁶ Jooste, supra note 89, at 442.

¹⁵⁷ Jooste, supra note 44, at 289.

by a couple of senior executives, does this make the barman an 'insider'?¹⁵⁸ From the preceding discussions, it was seen that the prosecution does not need to establish a business or professional relationship between the individual and the company,¹⁵⁹ it therefore seems as though the wording of this section is potentially wide enough to cover this situation. According to the strict wording of this section, it could be argued that the barman did get the information by virtue of his employment. However, if a functional link was required between a person's employment, office or profession and the company or the securities to which the information relates, then the barman in the above example would not be caught as a primary insider.¹⁶⁰ However, it is unclear whether such a link is required.¹⁶¹

It seems that if no functional link is required, the prohibition contained in the Act would apply to anyone in possession of inside information, not taking into account how he or she came into possession of that information. Rider & Ashe, commenting on the English position,¹⁶² are of the opinion that 'office cleaners, temporary secretaries, postmen, company printers and many others could potentially be regarded as having access to information by virtue of their employment.'¹⁶³ However, they are of the opinion, that if 'in the course of cleaning the issuer's windows, a window cleaner obtains inside information, he can hardly be said to have gained access to it by virtue of his employment.'¹⁶⁴ In this situation, Rider & Ashe feel that the 'information will have been gained through a frolic of his own and have come to him accidentally in the course of his employment.'¹⁶⁵

¹⁵⁸ Jooste, *supra* note 44, at 289.

¹⁵⁹ *Ibid.*

¹⁶⁰ *Ibid.*

¹⁶¹ *Ibid.*

¹⁶² Section 57(2)(a) of the Criminal Justice Act 1993.

¹⁶³ Barry Rider & Michael Ashe, *Insider Crime: The New Law* (1993) at 41.

¹⁶⁴ *Ibid.*

¹⁶⁵ *Ibid.*

From the above, it seems as though the legislature did not necessarily intend this section to be so widely construed. The theory behind the design of the section seems to be that the legislature's intention, when attempting to define an 'insider', was not to make anyone in possession of inside information to be considered an insider and that accidentally getting inside information should therefore not be covered. It is submitted that an 'insider' should not be just anyone with inside information but that it should rather depend on how he or she came into possession of that information, in other words, it is felt that there should be some form of transmission of the information. It is therefore submitted that the design of the section is in fact to pass on the information as opposed to accidentally gaining possession of such information. If X, for example, witnesses an explosion while driving past a factory and therefore knowing that the particular share prices in the company will drop, sells his shares before this information has been made public, X is not an insider as the inside information was not passed on to him. What then is the rationale behind the barman getting caught in the first example and not X? It could therefore be argued that a further theme of the Act is the theory that it is not just anyone in possession of inside information who will fall within the ambit of s 72(a)(ii) as it will depend on how that person got the information, actual passing on of the inside information being a necessary element of the offence. In terms of this theory, some sort of actual transmission of the information is required for a person to be considered an 'insider'. Inside information could easily pass on to a lawyer, for example, as although not connected with the company, he may still have gained direct access to the information as a result of his position and not 'through a frolic of his own'.

As already discussed above, s 72 provides for a third category of 'insider', which covers the secondary insider or 'tippee', being a person who has inside information and who knows that the direct or indirect source of the information was a primary insider. Therefore a person who overhears inside information will have that information as an insider if he knows that it is inside information and

knows that it is from an inside source.¹⁶⁶ This is because this provision is wide enough to include “casual” or “fortuitous” insiders ‘whose informational superiority derived from information that they accidentally stumbled upon or overheard.’¹⁶⁷ It is therefore important to note that the barman in the above example would have been caught as a ‘tippee’, in terms of this third category, if the prosecution could prove he knew that those persons were an inside source.¹⁶⁸ In terms of this third category, it is similarly submitted that this category should not be so widely construed so as to include accidentally or inadvertently coming across inside information.

It is therefore submitted that a theme in the current Act, in relation to primary insider dealing, is that the legislature is more focused on how the information came to be transmitted to the present holder, whereas in relation to secondary insider dealing, the focus is on the fact that it was transmitted.¹⁶⁹ However, if the legislature really did intend that the information have been passed in order to be classified as a ‘by virtue’ insider, then the question needs to be asked as to why this second category of ‘insider’ is needed at all? Wouldn’t ‘tipping’ have been enough?

¹⁶⁶ Rider & Ashe, *supra* note 163, at 46.

¹⁶⁷ Osode, *supra* note 82, at 245.

¹⁶⁸ Blackman *et al*, *supra* note 1, at 5-394-16.

¹⁶⁹ Davies has come to this conclusion regarding sections 57(1) and (2) of the CJA 1993, however it is submitted that the same can be said regarding South Africa’s present Act (Davies, *supra* note 13, at 467).

CHAPTER 4: 'INSIDE INFORMATION'

4.1 AN OVERVIEW

A common element of the offences under the Act, as was the case with the Insider Trading Act, is that in order to commit an offence, the accused must have 'inside information'. The requirement that information be 'inside information' is therefore an essential element of the offences. Under the Act, 'inside information' has four characteristics.¹⁷⁰ Section 72 provides that it is information which: (1) relates to any security listed on a regulated market; (2) is specific or precise; (3) has not been made public; and (4) if it were made public would be likely to have a material effect on the price or value of any securities. As a result of this definition being almost identical to that of the Insider Trading Act,¹⁷¹ any reference in this dissertation to the 'current definition', is also intended to cover the definition that which was previously provided for under the Insider Trading Act.

Previously, s 233 did not provide a definition of 'inside information' but rather spoke of information, which if published might materially affect the price of shares. Price-sensitive information had to relate to 'a transaction or proposed transaction of the company or of the affairs of the company'.¹⁷² Inside information under s 440F, was referred to as 'unpublished price-sensitive information' and had the following elements: (1) the information had to relate to matters in respect of the internal affairs of a particular company or its operations, assets, earning power or involvement in a take-over;¹⁷³ (2) it must not have been

¹⁷⁰ Section 72 of the Act.

¹⁷¹ Section 1(vii) of the Insider Trading Act defined "inside information" to mean 'specific or precise information which has not been made public and which- (a) is obtained or learned as an insider; and (b) if it were made public would be likely to have a material effect on the price or value of any securities or financial instrument.'

¹⁷² Section 233 of the 1973 Act.

¹⁷³ Section 440F(2)(a)(i).

generally available to the reasonable investor in the relevant markets for that security¹⁷⁴ and (3) had to reasonably be expected to affect materially the price of such security if it were generally available.¹⁷⁵

4.2 INFORMATION NEED ONLY RELATE TO SECURITIES GENERALLY OR ISSUERS OF SECURITIES GENERALLY

As a consequence of s 233 having required that price-sensitive information relate to 'a transaction or proposed transaction of the company or of the affairs of the company', the prohibition did not cover market information, being 'information about the market for a company's securities rather than about the company itself.'¹⁷⁶ Section 440F required that price-sensitive information related 'to matters in respect of the internal affairs of a particular company or its operation, assets, earning power or involvement as offeror or offeree in an affected transaction or proposed affected transaction'¹⁷⁷ and therefore also excluded information which related to the industry in which the company operated, unless that information was in respect of the company's earning powers.¹⁷⁸

From the above it can be seen that the aim of both s 233 and s 440F was therefore to cover information, which related to a specific sector as well as to a specific security. Information about a substantial increase or cut in the profits of a company is an example of information, which relates to an issuer of securities, as it clearly has its source within the organisation.¹⁷⁹ This must be seen in contrast with the current definition where information relating to securities

¹⁷⁴ Section 440F(2)(a)(ii).

¹⁷⁵ Section 440F(2)(a)(iii).

¹⁷⁶ Jooste, *supra* note 31, at 594-5.

¹⁷⁷ Section 440F(2)(a)(i).

¹⁷⁸ Luiz, *supra* note 66, at 142.

¹⁷⁹ Rider & Ashe, *supra* note 163, at 30.

generally, or issuers of securities generally would qualify as inside information.¹⁸⁰ This wider approach would include, for example, confidential information of a particular government economic policy, which would impact on the market generally.¹⁸¹ It is submitted that the fact that information may still be 'inside information' although it has nothing specifically to do with a company or its shares but rather to the industry in which it participates, is an important theme of the Act, having extended liability for the crime of insider trading.

4.3 'MATERIAL EFFECT'

As mentioned above, to qualify as 'inside information' for the purposes of the Act, the information in question must be such that, if made public, 'would be likely to have a material effect on the price or value of any securities'.¹⁸² Materiality was also similarly required under the previous insider trading laws¹⁸³ and therefore is a further common theme of the insider trading laws.

4.4 'SPECIFIC OR PRECISE'

To qualify as 'inside information' under the Act, it is a requirement that the information is specific or precise.¹⁸⁴ This was also a requirement under the Insider Trading Act.¹⁸⁵ However, neither s 233 nor s 440F expressly provided for this requirement. According to Osode, these words have been used in order to exclude market transactions that are based on information that is 'vague' or 'general'.¹⁸⁶ Information that suggests future scenarios or possibilities with no

¹⁸⁰ Jooste, *supra* note 44, at 290.

¹⁸¹ Rider & Ashe, *supra* note 163, at 32.

¹⁸² Section 72(b) of the Act.

¹⁸³ Section 233, s 440F and s1(vii) of the Insider Trading Act.

¹⁸⁴ Section 72 of the Act.

¹⁸⁵ Section 1(vii) of the Insider Trading Act.

¹⁸⁶ Osode, *supra* note 82, at 243.

'certain likelihood' of becoming reality would also be excluded.¹⁸⁷ It is thought that the effect of the restriction imposed by the use of these words is to prevent directors and senior managers of the company as well as analysts from falling foul of the legislation simply because they have 'generalised information advantages over other investors, arising from their position in the one case and the effort they have exerted in the other.'¹⁸⁸ The purpose of the 'specific or precise' requirement, as expressed by Osode, is to 'assure market participants that transactions or conduct based on rumours, suspicion, conjecture, speculation or a combination thereof, do not fall within the purview of the Act.'¹⁸⁹ It is therefore submitted that the exclusion of generalised information advantages and information based on speculation or rumours represents important general themes underlying the 'specific or precise' requirement of the Act.

4.5 'MADE PUBLIC'

Previously, s 233 prohibited dealing on the basis of price-sensitive information, which had 'not been publicly announced on a stock exchange or in a newspaper or through the medium of radio or television.'¹⁹⁰ However, as any public announcement would satisfy this requirement, an insider could have traded on the basis of price sensitive information shortly after or simultaneously with publication, in other words, before share prices had moved in response to that information.¹⁹¹ Publicizing the relevant information in 'an obscure part of some minor local newspaper' or announcing it on a minor local radio programme with limited listenership could also suffice, for example.¹⁹² Therefore, although the

¹⁸⁷ Osode, *supra* note 82, at 243.

¹⁸⁸ Davies, *supra* note 13, at 461.

¹⁸⁹ Osode, *supra* note 82, at 243.

¹⁹⁰ Jooste, *supra* note 31, at 594.

¹⁹¹ Jooste, *supra* note 55, at 249.

¹⁹² Jooste, *supra* note 55, at 249.

information was 'published', it may not have reached the minds of investors,¹⁹³ which would have left the insider free to be among the first to deal in the relevant shares and in this way could have effectively avoided the application of s 233.¹⁹⁴

Section 440F closed this loophole by regarding price-sensitive information as published only after it had been made 'generally available to the reasonable investor in the relevant markets for that security'.¹⁹⁵ It would only be 'generally available' in terms of s 440F(2)(b) if such steps had been taken, and such time elapsed, that it could reasonably have been expected that the information was or should have been known to the investor.¹⁹⁶ Section 440F(2)(b) therefore recognised the fact that outsiders need an opportunity to digest the information.¹⁹⁷ By not requiring publication in any particular manner, s 440F(2)(b) broadened the range of acceptable modes of publication.¹⁹⁸ However, one of the deficiencies of s 440F¹⁹⁹ was that the question as to whether or not price-sensitive information had been made public was determined on the basis of an objective 'reasonable investor' test, which led to uncertainties as to when price-sensitive information had been made public so as to permit its use.²⁰⁰

As with the above provisions, it is a requirement under the Act²⁰¹ (as was the case with the Insider Trading Act)²⁰² that in order to qualify as 'inside information' the information must not yet have been made public. From the above, it can be seen that although the 'made public' requirement has been a common theme of the various insider-trading laws, the various enactments have differed as to what

¹⁹³ Jooste, *supra* note 55, at 249.

¹⁹⁴ *Ibid.*

¹⁹⁵ Section 440F(2)(ii).

¹⁹⁶ Section 440F(2)(b).

¹⁹⁷ Jooste, *supra* note 31, at 593..

¹⁹⁸ *Ibid* at 594.

¹⁹⁹ Blackman *et al*, *supra* note 1, at 5-394-12.

²⁰⁰ Jooste, *supra* note 44, at 291.

²⁰¹ Section 72 of the Act.

²⁰² Section 1(vii) of the Insider Trading Act.

this would entail. Both the Act and the Insider Trading Act reflect a change in the legislatures approach to this ‘non-public’ requirement. The legislature has moved away from using the ‘reasonable investor’ test and leaving the problem to be solved by the courts on a case-by-case basis so as to introduce a measure of certainty.²⁰³

Without limiting the circumstances in which information shall be regarded as having been made public, s 74(1) of the Act stipulates four alternative situations where the information ‘shall’ be regarded as having been made public. Section 74(1) regards ‘inside information’ as having been made ‘public’ in circumstances which include, but are not limited to, the following: (a) when the information is published in accordance with the rules of the relevant regulated market for the purposes of informing clients and their professional advisers; or (b) when the information is contained in records which by virtue of any enactment are open to inspection by the public; or (c) when the information can be readily acquired by those likely to deal in any listed securities (i) to which the information relates; or (ii) of an issuer to which the information relates; or (d) it is derived from information which has been made public. Section 74(1)(d) is intended to ‘protect analysts who derive insights into a company’s prospects which are not shared by the market generally...where those insights are derived from the intensive and intelligent study of information which has been made public.’²⁰⁴ Section 74(1) is almost identical to the corresponding provision that was provided in s 3(1) of the Insider Trading Act.²⁰⁵

²⁰³ Jooste, *supra* note 44, at 291.

²⁰⁴ Davies, *supra* note 13, at 462.

²⁰⁵ Section 3(1) is the corresponding section of the repealed Insider Trading Act, which provided the following guidance in determining whether information will be regarded as having been made public: it provided that ‘information shall be regarded as having been made public in circumstances which include but are not limited to those when –

- (a) it is published in accordance with the rules of the relevant regulated market for the purpose of informing investors and their professional advisers; or
- (b) it is contained in records maintained by the relevant statutory regulator which by virtue of any enactment are open to inspection by the public; or
- (c) it can be readily acquired by those likely to deal in any securities or financial instruments -
- (i) to which the information relates; or

Section 74(2) of the Act, lists three situations where despite the fact that these circumstances might suggest that the information has not been made public, the information may still be regarded as having been made public. Section 74(2) provides that inside information which would otherwise be regarded as having been made public must still be so regarded even though (a) it can be acquired only by persons exercising diligence, or observation, or having expertise; (b) it is communicated only on payment of a fee; or (c) it is only published outside the Republic. According to Gower, when commenting on the similar United Kingdom legislation, the circumstances described in the above subsections do not prevent the court from holding the information to have been made public, but whether a court will do so will depend on the circumstances of the case as a whole.²⁰⁶ This provision is also almost identical to the corresponding provision that was provided in s 3(2) of the Insider Trading Act.²⁰⁷ However, s 3(2)(b), in addition provided for the situation where inside information may have been regarded as having been made public even though it was communicated to a section of the public and not to the public at large. It is submitted that this exclusion from the Act is probably a result of the legislature's aim to 'toughen up' on the previous legislation as well as making it fairer.

In summary, it can be seen that an important theme of the Act is the fact that information must be of a non-public nature in order to ground liability. Once made public however, the price-sensitive information is stripped of its non-public nature and therefore any subsequent dealing on the basis of such information is permitted. This is a common theme of the different insider trading laws, despite

(ii) of an issuer to which the information relates; or
(d) it is derived from information which has been made public.'

²⁰⁶ Davies, *supra* note 13, at 462, fn 5.

²⁰⁷ Section 3(2) of the Insider Trading Act provided that 'inside information may be regarded as having been made public even though-

(a) it can be acquired only by persons exercising diligence, or expertise or by observation;
(b) it is communicated to a section of the public and not to the public at large;
(c) it is communicated only on payment of a fee; or
(d) it is only published outside the Republic.'

the change in approach when determining whether or not price-sensitive information has in fact been made public.

4.6 IS THE ACT DOING WHAT IT OUGHT TO BE DOING IN TERMS OF ITS DEFINITIONS OF 'INSIDER' AND 'INSIDE INFORMATION'?

The interconnected definitions of 'inside information' and 'insider' under the Act, as was the case in terms of the Insider Trading Act, have been criticised as being 'cumbersome and counter-intuitive'.²⁰⁸ The definitions have been described as 'circular' in that 'to know whether information is 'inside information' one has to know who an 'insider' is; and to know who an 'insider' is, one has to know what 'inside information' is.' 'Inside information' is information 'which is obtained or learned as an 'insider'; and an 'insider' is 'a person who has 'inside information'.²⁰⁹ As a result of the fact that the provisions impose both criminal and civil liability which turns on the meaning of 'inside information', the Act (as with the Insider Trading Act) has been described as 'fundamentally incoherent'.²¹⁰

As a result of the lack of clarity regarding the above terms, it could be argued that the act is not doing what it ought to be doing. However, it is submitted that the interconnected definitions could just be more as an odd feature, in that they seem to work, despite this lack of clarity.

²⁰⁸ Jooste, *supra* note 89, at 438.

²⁰⁹ *Ibid.*

²¹⁰ *Ibid.*

CHAPTER 5: KNOWLEDGE

5.1 THE 'KNOWLEDGE' REQUIREMENT

There was some doubt as to whether the reference to 'knowledge' in s 233 meant that *mens rea* was an essential element of the crime of insider trading.²¹¹ However, according to Jooste, the use of the word 'knowingly' in s 440F(1) was a clear indication that the requirement of 'knowledge' was an essential element of the crime.²¹² In order to assist the prosecution in proving the offence, s 440F(3) contained two rebuttable presumptions.²¹³ In terms of the first, once the prosecution had proved that 'the accused was in possession of unpublished price-sensitive information in respect of the security in question at the time of the alleged commission of the offence', he or she was deemed to have knowingly dealt on the basis of such information, unless the contrary was proved.²¹⁴ In terms of the second, if the prosecution had proved that the unpublished price-sensitive information was obtained through espionage, theft, bribery, fraud, misrepresentation or any other wrongful method, he was deemed, unless the contrary was proved, to have known that such information was obtained in this manner.²¹⁵ Therefore, in order to rebut either of the presumptions, the accused had to produce evidence proving that he did not know that his act was contrary to law.²¹⁶ If, for example, he or she was unaware of the existence of s 440F or was wrongfully advised as to the law, he or she could not be convicted of the crime as a result of his lack of knowledge of unlawfulness.²¹⁷

Knowledge is also a common requirement of the offences (and civil wrongs)

²¹¹ Jooste, *supra* note 31, at 592.

²¹² *Ibid.*

²¹³ Botha, *supra* note 12, at 13.

²¹⁴ Section 440F(3).

²¹⁵ Section 440F(3)(b) and (ii).

²¹⁶ Jooste, *supra* note 31, at 592.

²¹⁷ *Ibid.*

under the Act,²¹⁸ in that an insider suspected of committing an offence must 'know' that he or she has 'inside information'. 'Knowledge' is therefore a prerequisite for both civil and criminal liability.²¹⁹ It must be proved that the offender knew that the information came from an inside source, in other words, that he or she fell within one of other of the three categories of 'insider'.²²⁰ The requirement of knowledge is the same under both the new provisions and the repealed Insider Trading Act.²²¹ In criminal proceedings, the prosecution must prove knowledge on part of the alleged offender beyond reasonable doubt, whereas in civil proceedings, knowledge must be proved on a balance of probabilities.²²² From the above it can be seen, taking into account the some doubt that was expressed with s 233, that the requirement of 'knowledge' on the part of the offender has been a common element of South Africa's insider trading legislation, at least since s 440F was enacted.

As mentioned above, Insider trading is an extremely difficult crime to prove.²²³ The underlying act of buying or selling securities is a perfectly legal activity.²²⁴ 'It is only what is in the mind of the trader that can make this legal activity a prohibited act of insider trading.'²²⁵ Proving that a defendant has acted knowingly creates a difficulty for the prosecution, as many of the facts to be established will be matters of judgement and therefore hard to prove.²²⁶ For example, determining whether the insider knew that the information was 'specific or precise' and whether it has been 'made public'.²²⁷ Direct evidence of insider

²¹⁸ Sections 73(1)(a), 73(2)(a), 73(3)(a) and 73(4) of the Act.

²¹⁹ Osode, *supra* note 82, at 248.

²²⁰ Section 72 of the Act.

²²¹ See ss 2(1), 6(1) and 6(2) of the Insider Trading Act; Jooste, *supra* note 89, at 440, fn 53.

²²² Osode, *supra* note 82, at 249.

²²³ Thomas C. Newkirk & Melissa A. Robertson 'Insider Trading: A U.S. Perspective' at 9, paper delivered on the 19th September at the 16th International Symposium on Economic Crime, Jesus College, Cambridge, England. Available at: <http://www.sec.gov/news/speech/speecharchive/1998/spch.htm> [visited: 03/08/2008].

²²⁴ *Ibid.*

²²⁵ *Ibid.*; see the discussion on the problems of proving the knowledge requirement discussed above.

²²⁶ Blackman *et al*, *supra* note 1, at 5-394-21.

²²⁷ Jooste, *supra* note 89, at 443.

trading is also considered to be rare as there is no physical evidence that can be scientifically linked to a perpetrator.²²⁸ Unless an insider trader confesses his knowledge in some admissible form,²²⁹ knowledge will be an inference drawn from circumstantial evidence.²³⁰ The investigation of the case and the proof that is needed requires examining inherently innocent events, such as: meetings in restaurants, telephone calls, relationships between people and trading patterns.²³¹

5.2 IS THE ACT DOING WHAT IT OUGHT TO BE DOING VIA THE KNOWLEDGE REQUIREMENT?

On inspection of s 172 of the Act, Jooste is of the opinion that if a primary insider is required to 'know' he or she has 'inside information', he or she must know the following elements: '(i) that it is 'specific or precise information', (ii) that it has not been made public, (iii) that they have obtained or learned of the information 'through' their position, and (iv) that 'if [the information] were made public' it 'would be likely to have a material effect on the price or value of any securities or financial instruments'.²³² In addition to the above, secondary insiders must know that the direct or indirect source of the information was a primary insider.²³³ According to Jooste, only the subjective appreciation of the above facts will do and therefore if an accused thinks, even if unreasonable, that the information is public, he does not commit the offence.²³⁴ The question as to whether the information has been made 'public' has its own set of difficulties.²³⁵ The difficulty stems from the fact that s 74(1) merely provides for certain circumstances, in which 'information shall be regarded as having been made

²²⁸ Newkirk & Robertson, *supra* note 223 at 9.

²²⁹ *Ibid.*

²³⁰ Douglas M Branson 'Insider Trading – Part II' (1982) *Journal of Business Law* 413 at 418.

²³¹ Newkirk & Robertson, *supra* note 223, at 9.

²³² Jooste, *supra* note 89, at 442.

²³³ *Ibid.*

²³⁴ *Ibid.* at 443.

²³⁵ *Ibid.* at 442.

public' which are not limited to the specified circumstances.²³⁶ In addition, experts may disagree as to whether the information was such that 'if it were made public would have a material effect on the price or value of any securities or financial instrument'.²³⁷

It does not matter whether the primary insider has consciously communicated the information to the secondary insider.²³⁸ Even if the secondary insider dealer has obtained the information indirectly, he would fall within the scope of the Act, provided he obtained the information from an inside source.²³⁹ It is thought that in cases where the information came indirectly from the primary insider to the suspect via a chain of communications, this requirement would be particularly difficult to meet.²⁴⁰ This would be the case when the prosecution would have to prove that a 'sub-tippee' or a 'sub-sub-tippee' knew that the ultimate source of the information was a primary insider.²⁴¹

As a result of the above-mentioned elements that a person needs to 'know' in relation to the 'inside information', a person may be in possession of information but may not necessarily know that it is 'inside information'.²⁴² In this situation a person will not be subject to the prohibition on insider trading as he or she must know the above elements. It is therefore submitted that the present Act may not be doing what it ought to be doing in respect of its formulation of the knowledge requirement, especially since it is a recurring theme throughout the Act. This stems from the fact that it could be very difficult for the prosecution to prove that a person truly believed that the information had been made public. As it is necessary in criminal proceedings for the prosecution to prove beyond

²³⁶ Jooste, *supra* note 89 at 443.

²³⁷ *Ibid.*

²³⁸ *Ibid.*

²³⁹ *Ibid.*

²⁴⁰ *Ibid.*

²⁴¹ *Ibid.*

²⁴² Blackman *et al*, *supra* note 1, at 5-394-21.

reasonable doubt all the elements of the crime of insider trading, any doubt as to whether the alleged offender knew that the information was, for example, specific or precise would lead to an acquittal. However, as will be discussed, there is no need to prove that a person in fact dealt on the basis of the information, only that he or she dealt while in possession of the inside information.

CHAPTER 6: THE POLICY GOAL OF DETERRENCE

Osode, when commenting on the provisions of the Insider Trading Act, was of the opinion that Parliament appeared to have 'been preoccupied or fixated solely on the policy objective of deterrence.'²⁴³ It has been thought that a deterrence effect is necessary as a result of the difficulties of securing successful prosecutions for the crime.²⁴⁴ It is thought that the increasing probability and cost of being caught deters market participants from engaging in insider trading.²⁴⁵ However, Osode was also of the view that 'single-minded and uncritical commitment to the policy goal of deterrence is the source of the many flaws in the Act.'²⁴⁶ He further feels that the Insider Trading Act did nothing to promote the policy goals of corporate compensation and market efficiency.²⁴⁷ It is submitted that the legislature, when drafting the current Act, has similarly and to a greater extent, fixated on this policy objective. As the deterrent effect can be seen throughout the provisions of the Act, it can therefore be said to represent an important theme in itself.

The penalty

It is submitted that the existing penalty for a contravention of the Act (a fine not exceeding R50 million or imprisonment for a period not exceeding ten years or both such a fine and imprisonment)²⁴⁸ is a clear indication of the legislature's focus on the deterrent effect. This is also evident in the civil context, where the Act provides for punitive penalties up to three times the profit gained or loss

²⁴³ Osode, supra note 82, at 262.

²⁴⁴ Genesis, supra note 4, at 14.

²⁴⁵ *Ibid.*

²⁴⁶ Osode, supra note 82, at 263. Osode is referring to the Insider Trading Act, however there seems to be no reason why this comment should not apply equally to the present Act.

²⁴⁷ *Ibid.*

²⁴⁸ Section 115(a) of the Act.

avoided by the insider trading.²⁴⁹ However, as 'no differentiation is made in the penalty provision between the acts of the actual insider trading and those of encouragement, discouragement or disclosure leading to same,'²⁵⁰ the current penalty may be viewed as draconian.²⁵¹ According to Osode, the actual insider trading is a class of its own and that the acts ought to be differentiated as a result of the gravity of the assault that each constitutes to the fairness, integrity and efficiency of the financial marketplace or to individual investors.²⁵² His argument is based on the fact that 'conviction and punishment for the proscribed acts of encouragement, discouragement or disclosure are not made contingent upon the offender having received some benefit as a result and/or upon insider trading having in fact occurred as a result of the offender's act.'²⁵³ In response to Osode's views, although to a certain extent convincing, it is submitted that one must also bear in mind that in these circumstance's the offender could just as likely in fact received such a benefit with the effect that one can never be sure whether a person who has been 'tipped off' is any less guilty than the true insider.

²⁴⁹ Sections 77(1)(ii), 77(2)(ii), 77(3)(ii) and 77(4)(b) of the Act. Section 6(3) of the Insider Trading Act provided for similar punitive damages as does the new Act, in terms of which an individual may be held 'liable at the suit of the Financial Services Board to pay to the Financial Services Board such sum determined in the discretion of the court but not exceeding three times the amount calculated in terms of s (4)(a)(i), together with all commission or consideration for disclosing, encouraging, discouraging or dealing.'

²⁵⁰ Osode, *supra* note 82, at 246.

²⁵¹ *Ibid.* Osode is referring to the penalties that were prescribed under the Insider Trading Act, however his comments will apply equally to the penalties prescribed under the current Act.

²⁵² *Ibid.*

²⁵³ *Ibid.*

CHAPTER 7: OFFENCES

7.1 THE DEALING OFFENCE

The Act makes it an offence for an insider, knowing that he or she has inside information, to deal (directly or indirectly) for his or her own account or for any other person in the securities listed on a regulated market to which the information relates or which are likely to be affected by it.²⁵⁴ For civil liability to arise, it is in addition required that an insider makes a profit or would have made a profit if the securities had been sold at any stage, or avoids a loss, through such dealing.²⁵⁵

7.1.2 DEALING 'DIRECTLY OR INDIRECTLY OR THROUGH AN AGENT'

The Insider Trading Act, as did s 440F(1) and s 233, rendered insiders liable if they dealt 'directly or indirectly'.²⁵⁶ It has been said that this reference 'obviously covers dealing through an agent',²⁵⁷ such as a stockbroker, as well as covering the acquiring and exercising of options and pre-emption rights relating to shares or debentures.²⁵⁸ Direct or indirect dealings are similarly outlawed under the Act, which renders an insider liable (both criminally and civilly) for the offence of 'dealing on one's own account', if they deal 'directly or indirectly or through an agent'.²⁵⁹ The offence of 'dealing on someone else's account' covers dealing

²⁵⁴ See ss 73(1)(a); 77(1); 73(2)(a) and 77(2) of the Act. Liability for the dealing offence is however subject to the insider being unable to prove one of the defences provided by the Act. The dealing offence was previously provided for in ss 2(1)(a) and 6(1)(a) of the Insider Trading Act.

²⁵⁵ See ss 77(1)(b) and 77(2)(b) of the Act.

²⁵⁶ Section 2(1)(a) of the Insider Trading Act.

²⁵⁷ Jooste, *supra* note 44, at 293.

²⁵⁸ Jooste, *supra* note 31, at 593.

²⁵⁹ Section 73(1)(a) of the Act.

'directly or indirectly' but does not mention dealing through an agent.²⁶⁰ There was no reference to dealing 'through an agent' under the Insider Trading Act.

From the above it can be seen that the prohibition on dealing 'directly or indirectly' has been a common feature of South Africa's anti-insider trading provisions since 1973. It was assumed that references to dealing 'indirectly' covered dealing through an agent, for example, a stockbroker.²⁶¹ However, since the enactment of the Act, it seems as though the reference to 'indirectly' merely covers the acquiring and exercising of options and pre-emption rights relating to shares or debentures and not that of dealing through a agent. According to Jooste, 'it appears that the insertion of the words 'through an agent' indicates that the legislature did not regard dealing through an agent as being clearly implied in the word 'indirectly'.'²⁶²

7.2 THE PROHIBITION OF CONDUCT WHICH CAN LOOSELY BE DESCRIBED AS CONSTITUTING THE AIDING AND ABETTING OF INSIDER TRADING AND THE REQUIREMENT OF DEALING

The introduction of the Insider Trading Act had the effect of clarifying what types of behaviour constitute insider trading and in doing so considerably broadened the range of offences that had previously existed.²⁶³ It did so by creating two new offences, that of 'encouraging' or 'discouraging'; and 'disclosing'.²⁶⁴ With the exception of the 'discouraging' offence, civil liability can arise from the same

²⁶⁰ Section 73(1)(a) of the Act.

²⁶¹ Blackman *et al*, supra note 1, at 5-394-23.

²⁶² Jooste, supra note 89, at 450.

²⁶³ Blackman *et al*, supra note 1, at 5-394-10.

²⁶⁴ Sections 2(1)(b) of the Insider Trading Act provided criminal liability for the 'encouraging' or 'discouraging' offence; s 6(2)(b) provided civil liability for the 'encouraging' offence only. Sections 2(2) and 6(2)(a) provided criminal and civil liability for that 'improper disclosure' offence respectively.

acts that can give rise to criminal liability.²⁶⁵ As previously mentioned, the Act prohibits the same forms of conduct, as did the Insider Trading Act.²⁶⁶ In terms of the new offences, the Act therefore imposes liability on insiders who, knowing they have inside information relating to particular securities, disclose²⁶⁷ the inside information to others, encourage²⁶⁸ others to deal in such securities or discourage²⁶⁹ others from dealing in such securities.

7.3 THE PREVIOUS POSITION UNDER S 233 AND S 440F

Previously, an insider was not prohibited under either s 233 or s 440F from making any hints or recommendations to an outsider on the basis of the inside information.²⁷⁰ Jooste considered this to be a glaring flaw in the legislation.²⁷¹ However, under the present Act, the insider would be liable under the 'encouraging' or 'discouraging' offence.²⁷² As s 440F extended the prohibition to include 'tippees', a tippee who dealt on the basis of the unpublished price sensitive information would have been found guilty of the dealing offence.²⁷³ However, the insider who passed on the information to the tippee would have not committed an offence, as he himself did not deal.²⁷⁴ This was the case even

²⁶⁵ Jooste, *supra* note 89, at 443. See ss 77(1), (2), (3), (4) of the Act.

²⁶⁶ However, it must be noted that the provisions of the various offences of the respective acts are not identical.

²⁶⁷ Sections 73(3)(a) of the Act provides for criminal liability on an 'insider who knows that he or she has inside information and who discloses the inside information to another person'. Section 77(3) similarly imposes civil liability for the same act.

²⁶⁸ Section 77(4) of the Act provides for civil liability on an 'insider who knows that he or she has inside information and who encourages or causes any other person to deal in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it is'.

²⁶⁹ Section 73(4) of the Act provides for criminal liability on an 'insider who knows that he or she has inside information and who encourages or causes another person to deal or discourages or stops another person from dealing in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it commits an offence.'

²⁷⁰ Jooste, *supra* note 55, at 250.

²⁷¹ *Ibid.*

²⁷² See ss 77(4) and 73(4) of the Act. The insider would also have been liable in terms of ss 2(1)(b) and 6(2)(b) of the repealed Insider Trading Act.

²⁷³ Jooste, *supra* note 31, at 596.

²⁷⁴ *Ibid.* In terms of the Act an insider would be found liable in terms of the 'disclosure offence'.

if the tippee dealt on the basis of the information.²⁷⁵ Under the Act, an insider who passes on the information to the 'tippee' will be liable for the improper disclosure offence.²⁷⁶

It was also a requirement under these previous insider trading laws, that the insider must have dealt (directly or indirectly) in order to commit an offence. Prior to the enactment of the Act, it was thought that if an individual dealt on behalf of or for the benefit of the primary insider, the primary insider would have been dealing indirectly and therefore he himself would have committed the offence.²⁷⁷ However, as previously discussed, the Act now contains the words 'directly or indirectly or through an agent'²⁷⁸ in relation to the dealing offence. It therefore seems as though the reference to dealing 'indirectly' in terms of the previous enactments was intended to merely cover the acquiring and exercising of options and pre-emption rights relating to shares or debentures and not that of dealing through a agent.

From the above it can be seen that the inclusion of the 'encouraging' or 'discouraging' offence and the 'disclosure' offence in both the repealed Insider Trading Act and the Act, represents a major extension of liability from what had existed previously. It also represents an important change in emphasis in South Africa's approach to combating insider trading. This stems from the fact that previously, emphasis was placed on the fact that a person must have dealt in order to be found liable and as a result it was not considered 'wrong' for an insider to pass on unpublished price sensitive information to a 'tippee' or to 'encourage' others to deal or to 'discourage' others from dealing in such securities as long as he himself did not deal.²⁷⁹ However, in terms of the

²⁷⁵ Jooste, *supra* note 31, at 596.

²⁷⁶ See ss 77(3) and 73(3)(a) of the Act. The insider would also have been liable in terms of ss 2(2) and 6(2)(a) of the repealed Insider Trading Act.

²⁷⁷ Jooste, *supra* note 31, at 596.

²⁷⁸ Section 73(1)(a) of the Act.

²⁷⁹ Jooste, *supra* note 31, at 596. In terms of the Act an insider would be found liable in terms of

present law, an insider may now be found liable without having to actually deal in the relevant securities or financial instruments.²⁸⁰ Greater emphasis is placed on the fact that an insider was in possession of the inside information rather than on whether or not he actually dealt on the basis of such information. This change in emphasis is represented by the fact that, at present, all the prosecution needs to show is that the offender knew that he or she was an insider and that he or she was in possession of inside information at the time he 'encouraged' or 'discouraged' dealing or 'disclosed' that information to another person who uses that information. The key here is the fact that the inside information came from an inside source.

In summary, it can be seen that the above represents an important change in emphasis as, since the introduction of the Insider Trading Act, the prohibition is 'not just on insider trading *per se* but also on certain related conduct which can loosely be described as constituting the aiding and abetting of insider trading.'²⁸¹

7.4 IT IS NOT A REQUIREMENT THAT THE ACCUSED HAVE BENEFITTED IN ANY WAY IN ORDER TO BE FOUND LIABLE UNDER THE ACT

In terms of s 233 an insider must have dealt to his or her advantage in order to be found criminally liable. Therefore if an insider did not benefit from his or her dealing but rather a third party received a benefit, the offence was not committed. However, in terms of s 440F it was no longer an essential element of the crime of insider trading that an insider must have dealt to his or her advantage.²⁸² Therefore if a person other than the insider benefited from the

the 'disclosure offence'.

²⁸⁰ Luiz, *supra* note 66, at 138.

²⁸¹ Osode, *supra* note 82, at 240.

²⁸² Jooste, *supra* note 55, at 249.

dealing in question, the offence would nevertheless have been committed.²⁸³

In order to be held criminally liable for the 'dealing' offence, the Act (as was the case with the Insider Trading Act²⁸⁴) does not require the accused to have made a profit or avoided a loss.²⁸⁵ Under the Insider Trading Act,²⁸⁶ civil liability for insider dealing only arose if the defendant had made a profit or avoided a loss through such dealing. The Act therefore represents a slight change in emphasis in this regard, requiring that the defendant have made a profit or would have made a profit if he or she had sold the securities at any stage, or avoided a loss through such dealing.²⁸⁷ The Act therefore provides for the situation where a profit has not been made but would have been made had the securities been sold.²⁸⁸ By closing a possible loophole that existed under the Insider Trading Act, the provisions of the Act are again indicative of the deterrence effect.

Liability for the encouraging or discouraging offence under the Act (as was the case with the Insider Trading Act²⁸⁹) is also not contingent upon the wrongdoer having received any financial or other reward for the illicit conduct.²⁹⁰ In other words, it is not relevant whether the advice was offered gratuitously or for personal gain. The same can be said regarding the disclosure offence.²⁹¹ Liability for the civil offences of encouraging and disclosure are similarly not contingent on the insider being remunerated in some way.²⁹²

²⁸³ Jooste, *supra* note 55, at 249.

²⁸⁴ Section 2(1)(a) of the Insider Trading Act; Blackman *et al*, *supra* note ? at 5-394-22.

²⁸⁵ Section 73(1)(a) of the Act; Jooste, *supra* note 89, at 444.

²⁸⁶ Section 6(1)(b) of the Insider Trading Act.

²⁸⁷ Section 77 of the Act.

²⁸⁸ Jooste, *supra* note 89, at 445.

²⁸⁹ Osode, *supra* note 82, at 242.

²⁹⁰ Jooste, *supra* note 89, fn 101.

²⁹¹ Osode, *supra* note 82, at 242; Jooste, *supra* note 89, at fn 101.

²⁹² Sections 73(3)(a) and 73(4); Jooste, *supra* note 89, at fn 101; However, any 'commission or consideration received' is claimable from the insider in terms of s 77(3)(b)(iv) and 77(4)(d) of the Act. The amounts referred to in s 77(4) only become payable if the tippee deals.

7.4.1 COMMON THEMES AND CHANGE IN EMPHASIS

From the above it can be seen that a common theme of the prohibition on insider trading (in relation to criminal liability) in South Africa since the enactment of section 440F, is that it is not an essential element of the dealing offence that the insider must have dealt to his or her advantage (by either gaining a profit or avoiding a loss).²⁹³ It was similarly shown that the encouraging and the disclosure defences can also be placed under this common theme as neither offence require that the wrongdoer must have received any financial or other reward for the illicit conduct in order to incur criminal or civil liability in terms of both the Insider Trading Act and the Act. This was also shown to be the case with the discouraging offence in relation to criminal liability. Further, the knowledge requirement, being a common element of the offences, in addition does not require it be shown that the alleged wrongdoer deliberately exploited the information for personal financial gain, in addition to proof of mere knowledge of the inside information.²⁹⁴ Therefore, unless an 'insider' is able to prove one of the provided defences, the mere possession of inside information and knowledge on the part of the alleged offender is sufficient to be found liable in terms of the Act (as was the case with the Insider Trading Act).

It is submitted that an important theme is that, although the criminal offences do not always require that the possession of inside information have resulted in any sort of advantage to the wrongdoer, the Act is based on the same basic idea as that of s 233. There still seems to be a worry about gaining an advantage when in possession of such information, which is not necessarily the gaining of a profit through the use of such information. By dispensing with the advantage requirement and therefore broadening the offences, the Act (as was the case with s 440F and the Insider Trading Act) has in fact made it easier for the

²⁹³ Jooste, *supra* note 55, at 249.

²⁹⁴ Osode, *supra* note 82, at 248.

prosecution to secure a conviction as it would no longer be an essential criteria of the crime that the prosecution prove any advantage or gain on the part of the offender.

7.5 IT IS NOT A REQUIREMENT THAT AN INDIVIDUAL MUST HAVE DEALT ON THE BASIS OF THE INSIDE INFORMATION TO BE GUILTY OF AN OFFENCE

Previously, in order to commit the dealing offence, s 440F(1)²⁹⁵ required the prosecution to have shown that a person actually dealt on the basis of the price-sensitive information in order to be found liable. This was due to the legislature having approached insider trading on the basis that ‘the receiving of the inside information was not, ipso facto, an offence’.²⁹⁶ There must have been actual dealing on the basis of the inside information in order to attract criminal liability,²⁹⁷ in that a person actually altered his or her position whilst in possession of such information.²⁹⁸ The mere possession of inside information was therefore not considered an actionable wrong in terms of the anti-insider trading provisions. As has already been mentioned, one of the rebuttable presumptions contained in s 440F(3)(a) was to the effect that once the prosecution had proved that ‘the accused was in possession of unpublished price-sensitive information in respect of the security in question at the time of the alleged commission of the offence’, he or she was deemed to have knowingly dealt on the basis of such information, unless the contrary was proved. However, the introduction of the Insider Trading Act meant that there was ‘no longer any need for the prosecution to show that the alleged offender dealt on the basis of the information.’²⁹⁹ In terms of s 2(1)(a),³⁰⁰ all that was needed to

²⁹⁵ Of the 1973 Act.

²⁹⁶ Jooste , supra note 31, at 596.

²⁹⁷ *Ibid.*

²⁹⁸ *Ibid.* at 593.

²⁹⁹ Luiz, supra note 66, at 138.

³⁰⁰ The Insider Trading Act.

be proved was that the offender knew that he or she was in possession of 'inside information' and that he or she dealt in the relevant securities.³⁰¹ There was no need for the prosecution to establish that possession of the information prompted the decision to deal.³⁰² This is an important theme and has been carried through in the provisions of the Act,³⁰³ which also does not require the prosecution to prove that the dealing was motivated by the inside information.³⁰⁴

The fact that it is not a requirement under the Act that an accused actually dealt on the basis of the inside information, as was submitted to be the case with the advantage requirement, seems to be based on the idea of expedience, in that by dropping this requirement and broadening the offence, it is then easier to secure a conviction. It is therefore submitted that the Act is still based on the same idea as that of s 233, although this idea has been moderated in order to try and make it easier to secure a conviction.

7.6 ABSTAINING FROM DEALING GIVES RISE TO NO CRIMINAL OR CIVIL LIABILITY

A person who refrains from dealing on the basis of the inside information is not covered under the Act and therefore cannot be held criminal or civil liability.³⁰⁵ This would be the case where an insider decides on the basis of inside information not to deal, when he would have dealt had he not possessed the information – because he acquired information that the securities will increase in value.³⁰⁶ This, in addition to being one of the main themes of the Act, is also a common theme that runs through all previous legislative attempts to combat

³⁰¹ Luiz, *supra* note 66, at 138.

³⁰² Blackman *et al*, *supra* note 1, at 5-394-23.

³⁰³ Sections 73(1)(a); 73(2)(a); 77(1) and 77(2) of the Act.

³⁰⁴ Davies, *supra* note 13, at 468.

³⁰⁵ Jooste, *supra* note 89, at 445.

³⁰⁶ Jooste, *supra* note 31, at 593.

insider trading. In regard to the same position in England, Gower states that it is difficult to defend this exclusion in principle 'since the loss of public confidence in the market will be as strong as in a case of dealing, if the news of the non-dealing emerges. The exclusion was presumably a pragmatic decision based on severe evidential problems which would face the prosecution in such a case.'³⁰⁷

7.7 PERSON ENCOURAGED MAY DEAL

A further important theme of the Act, as was the case under the Insider Trading Act, is that a person who is encouraged to deal without receiving any inside information is not guilty of the offence of insider dealing if he or she then subsequently deals.³⁰⁸ The insider who imparted the advice to the recipient to deal in specified securities (encouraged) will however be guilty of the encouragement offence.³⁰⁹ However, the recipient of such advice may only be found guilty of the dealing offence if he or she in fact received the inside information on which the advice was based (so as to be in actual possession of the information) and then subsequently dealt in the relevant securities.³¹⁰ If the recipient received the information when he/she was encouraged, the person who encouraged the recipient may in addition have committed the disclosure offence.³¹¹ Therefore the recipient of the advice or encouragement will only be liable if the inside information is passed on to him by the insider (who is in possession of the inside information).³¹² According to Jooste, it is unclear why liability should only arise if the inside information is passed on to the recipient.³¹³ He feels that this anomaly represents a serious flaw in the legislature's attempt

³⁰⁷ Davies, *supra* note 13, at 468.

³⁰⁸ Section 73(4) of the Act; Jooste, *supra* note 89, at 452.

³⁰⁹ Jooste, *supra* note 89, at 452.

³¹⁰ *Ibid.*

³¹¹ *Ibid.*

³¹² *Ibid.*

³¹³ *Ibid.*

to combat insider trading.³¹⁴

The fact that a person who is 'encouraged' may deal in the relevant securities without committing an offence seems to suggest that the legislature does not consider it a wrong of insider trading that a person can benefit from the fact that someone else is in possession of unpublished price-sensitive information as long as he was not in possession of it himself. It could however be argued that the inside information indirectly prompted him to deal, for example, a nudge or a wink from a managing director of a multi-million rand company indicating to a person that it would be to his advantage to buy or sell shares in that company. Is this not putting a person at an informational advantage over other investors? The director in this example has put the recipient in a position of ascendancy over investors, which is not justified by, any attributable to any industry or merit. This could be considered as an unfair advantage over other investors as fairness requires equality of opportunity, the inherent unfairness of the practice being the reason for prohibiting it.³¹⁵

In most cases it can be assumed that the recipient knows that a director is in possession of inside information as a result of his position and by heeding the advice, he can almost be assured that he will benefit from the fact that the director was in possession of such information. It seems that this would create an unfair playing field as the recipient will profit at other investors expense. However, the fact that no liability attaches to a person who deals when 'encouraged' to do so by an insider, could also be seen as a deterrent to insiders from abusing their position in that they will be liable for the imparting of advice whether or not that advice is heeded. It seems as though this is what the legislature hopes to be the effect of this provision so as to ensure the integrity of the securities market.

³¹⁴ Jooste, *supra* note 89, at 452.

³¹⁵ Blackman *et al*, *supra* note 1, at 5-378.

CHAPTER 12: THE DEFENCES

The defences to the various offences provided are thought to be necessary as there are genuinely times when an accused has done no wrong. As will be discussed below, the Act is in many respects indicative of a harsher line taken by the legislature in its attempt to improve on the previous legislation, as well as closing any loopholes that had previously existed. It is submitted that a worrying feature of the Act is that the legislature's attempt of 'toughening up' the provisions of the Insider Trading Act may have had the unintended effect of punishing the innocent. The following are examples of where this 'toughening up' is clearly evident in relation to the defences under the Act:

The accused 'only became an insider after he or she had given the instruction to deal to an authorised user and the instruction was not changed in any manner after he or she became an insider'

The enactment of the Act has resulted in the removal of the general, wider defence that was previously provided for under the Insider Trading Act; namely: where the accused 'would have acted in the same manner even without the inside information'.³¹⁶ The defence that he or she 'only became an insider after he or she had given the instruction to deal to an authorised user and the instruction was not changed in any manner after he or she became an insider' replaced this.³¹⁷ In terms of the Act, this defence is made available to an accused for the offences of 'dealing on one's own account'³¹⁸ and 'dealing on

³¹⁶ Section 4(1)(b) of the Insider Trading Act.

³¹⁷ Section 73(1)(b)(ii) of the Act.

³¹⁸ The defences to the offence of 'dealing on one's own account' are contained in s 73(1)(b) of the Act, which provides: 'An insider is, despite paragraph (a), not guilty of any offence contemplated in that paragraph if such insider proves on a balance of probabilities that he or she-

(i) was acting in pursuit of the completion of an affected transaction as defined in section 440A of the Companies Act;

(ii) only became an insider after he or she had given the instruction to deal to an authorised user

someone else's account'.³¹⁹ Osode found the old defence under the Insider Trading Act to be justifiable on two grounds. The first was that it applied to 'innocent', 'automatic' or 'non-discretionary' trades which did not feature any dishonesty on the defendant's part; and the second was that 'because the affected trades would have been concluded even if the defendant were not in possession of inside information, they cannot be properly regarded either as an affront to the integrity of the financial markets or as the cause of any of the unsavoury effects which insider trading is said to be capable of generating'.³²⁰

According to Jooste, the old defence would have covered the circumstances covered by the new defence but that the old one is undoubtedly wider than the new.³²¹ An example where (assuming the requisite *mens rea* was present) the dealer would have been protected by the old defence but not under the new defence, is where 'an individual who had price-sensitive information in relation to certain securities and sold them to meet pressing financial obligations, or who bought them in order to fulfil a pre-existing obligation to transfer them to another person'.³²² It is therefore submitted that it is clear that the old defence was originally provided to cater for situations where an accused was innocent and by replacing this defence with a harsher version, this innocence may be punished.

and the instruction was not changed in any manner after he or she became an insider.'

³¹⁹ The defences to the offence of 'dealing on someone else's account' are contained in s 73(2)(b) of the Act, which provides: 'An insider is, despite paragraph (a), not guilty of any offence contemplated in that paragraph if such insider proves on a balance of probabilities that he or she-

(i) is an authorised user and was acting on specific instructions from a client, save where the inside information was disclosed to him or her by that client;

(ii) was acting on behalf of a public sector body in pursuit of monetary policy, policies in respect of exchange rates, the management of public debt or external exchange reserves; or

(iii) was acting in pursuit of the completion of an affected transaction as defined in section 440A of the Companies Act;

(iv) only became an insider after he or she had given the instruction to deal to an authorised user and the instruction was not changed in any manner after he or she became an insider.'

³²⁰ Osode, *supra* note 82, at 251.

³²¹ Jooste, *supra* note 89, at 446-7.

³²² *Ibid* at 447.

An accused who 'is an authorised user and was acting on specific instructions from a client, save where the inside information was disclosed to him or her by that client'

Another defence that is provided for under the Act; in relation to the offence of 'dealing on someone else's account', is one that protects an accused who 'is an authorised user and was acting on specific instructions from a client, save where the inside information was disclosed to him or her by that client'.³²³ The relating defence under the Insider Trading Act, although similar, provided for the defence to be available to any 'individual' accused of the offence in question.³²⁴ The defence provided for under the Act, however, is only available to a person who is an 'authorised user'. An 'authorised user' has been defined as 'a person authorised by an exchange in terms of the exchange rules to perform such securities services as the exchange rules may permit'.³²⁵ Jooste is of the opinion that it appears as though 'the new defence is more limited in its application than the old one.'

The accused 'would have acted in the same manner even without the inside information'

The Act does not contain any defences in relation to the encouraging or discouraging offence. However, the Insider Trading Act provided a defence to an accused in the same situation where he or she 'would have acted in the same manner even without the inside information'.³²⁶ This defence also protected the accused who could have shown that the inside information did not prompt him to deal or to provide the encouragement or discouragement referred to in s 2(1)(b) of the Insider Trading Act, as he would have done so in the

³²³ Section 73(2)(b)(i) of the Act.

³²⁴ See s 4(1)(a) of the Insider Trading Act; Jooste, *supra* note 89, at 448.

³²⁵ Section 1 of the Act.

³²⁶ *Ibid.*

absence thereof.³²⁷ Jooste finds the removal of this defence to be harsh as 'there could have been genuine instances where the insider would have provided the encouragement or discouragement even without the inside information.'³²⁸ In terms of the UK legislation,³²⁹ only the act of 'encouragement' is included within its prohibition on insider trading and not that of 'discouragement' from dealing.³³⁰ However, the UK legislation provides a defence to the 'encouragement' offence, in terms of which 'an insider can only be convicted of the offence under section 55(2) if he or she had a reasonable cause to believe that the person on the receiving end of the encouragement would, in fact, engage in a transaction on the market.'³³¹ Therefore it seems as though the UK legislation, by providing such a defence, is providing for situations where an accused is genuinely innocent. With the identical offence in the SA legislation, however, this defence is not available. Here again the 'toughening up' of the Act has resulted in there being no defence to the 'encouraging or discouraging' offence in situations where an accused is genuinely innocent.

The accused 'disclosed the inside information because it was necessary to do so for the purpose of the proper performance of the functions of his or her employment, office or profession in circumstances unrelated to dealing in any security listed on a regulated market and that he or she at the same time disclosed that the information was inside information.'

The Act provides a defence to the disclosure offence, in terms which, an accused can avoid both criminal and civil liability, if he or she can prove 'on a balance of probabilities that he or she disclosed the inside information because it was necessary to do so for the purpose of the proper performance of the

³²⁷ Blackman *et al*, supra note 1 at 5-394- 25.

³²⁸ Jooste, supra note 89, at 450.

³²⁹ Section 52(2) of the Criminal Justice Act, 1993.

³³⁰ Osode, supra note 82, at 242.

³³¹ *Ibid.*

functions of his or her employment, office or profession in circumstances unrelated to dealing in any security listed on a regulated market and that he or she at the same time disclosed that the information was inside information.³³² The only difference between this defence and that of the Insider Trading Act is that the latter did not contain the words 'in circumstances unrelated to dealing in any security listed on a regulated market'.³³³ The insertion of the new wording could indicate the closing of a gaping hole that existed under the old defence.³³⁴ Jooste submits that this would be the case if the wording were inserted in order to 'prevent reliance on the exception by, for example, investment advisors whose 'employment, office or profession' would no doubt relate to 'dealing in any security listed on a regulated market'.³³⁵

The Insider Trading Act also provided a further defence to an individual who could prove on a balance of probabilities that he or she 'believed, on reasonable grounds that no person would deal in the securities or financial instruments as a result of such disclosure'.³³⁶ The Act however, does not provide such a defence. The subjectivity of the defence has been put forward as a possible reason for its removal, as it required determining the reasonableness of the accused's belief that 'no person would deal'.³³⁷ On the other hand, the removal of the offence has the effect that in a genuine situation, an 'innocent' person may be punished as he/she may genuinely have believed that no person would deal in the securities or financial instruments as a result of such disclosure.³³⁸

It is felt that the prohibition on insider trading should provide for situations in which an accused is genuinely innocent, despite the fact that he was in

³³² Section 73(3)(b) of the Act.

³³³ Section 4(2)(b) of the Insider Trading Act.

³³⁴ Jooste, *supra* note 89, at 449.

³³⁵ *Ibid.*

³³⁶ Section 4(2)(a) of the Insider Trading Act.

³³⁷ Jooste, *supra* note 89, at 449.

³³⁸ *Ibid.*

possession of price-sensitive information at the relevant time. Why should an insider who would have provided the encouragement or discouragement even without the inside information be punished but a person who has been encouraged to deal without receiving any inside information is not guilty of the offence of insider dealing if he or she then subsequently deals?

The above discussion is indicative of a change of emphasis regarding the prohibition on insider trading. The new defences were clearly intended to 'toughen up' and close any loopholes that existed in the previous act, indicating a harsher line taken by the legislature. The legislature, when drafting the Act, seemed to have placed an emphasis on limiting the application of many of the old defences or on their removal completely and as such represents a change in emphasis from the Insider Trading Act itself. It is assumed that such changes are aimed at a deterrent affect, however it is submitted that this should not overlook the fact that innocence may be punished as a consequence of 'toughening up'. This is especially important taking into account that the severe penalty for contravention of the Act and the fact that there is no differentiation of liability for the different acts and of primary and secondary insiders.

CHAPTER 9: NO TERRITORIAL CONNECTION REQUIRED

An important theme of the Act, as with the Insider Trading Act, is the fact that ‘no territorial connection is required between any element of the offences or civil wrongs and South Africa.’³³⁹ According to Jooste, ‘a foreign insider who knows that he or she has inside information and who deals outside South Africa in foreign securities listed on a foreign market to which the information relates could be prosecuted for the insider dealing offence in South Africa.’³⁴⁰

9.1 IS THE ACT DOING WHAT IT OUGHT TO BE DOING BY NOT REQUIRING ANY TERRITORIAL CONNECTION?

The fact that the Act, as was the case with the Insider Trading Act, has unlimited extra-territorial reach has been criticised as making no logical or financial sense.³⁴¹ Osode bases this criticism on mainly two reasons. In terms of the first, he is of the opinion that ‘where the offending transaction has taken place at a foreign market locale, any regulatory response by way of investigative and prosecutorial activity against the perpetrator only protects the integrity of that market, and it is unclear whether any benefits will redound therefrom to the South African markets.’³⁴² Secondly, Osode finds it ‘doubtful whether South Africa can afford the cost of conferring a statutory licence on the FSB to pursue its mission under the new Act on a global scale’.³⁴³ In the event that South Africa could afford these costs, it is thought that the costs will significantly outweigh the benefits.³⁴⁴

³³⁹ Jooste, *supra* note 89, at 453.

³⁴⁰ *Ibid.*

³⁴¹ Osode, *supra* note 82, at 260. Osode is referring to the Insider Trading Act, however there seems to be no reason why this comment should not apply equally to the present Act in regard to its extra-territorial reach.

³⁴² *Ibid.*

³⁴³ *Ibid.*

³⁴⁴ *Ibid.*

The United States of America is the only other jurisdiction to have 'explicitly sanctioned open-ended extra-territorial application of its securities laws by the famous Securities and Exchange Commission (SEC).'³⁴⁵ However, these laws are subject to important limitations.³⁴⁶ Contrary to the position in South Africa, there must be a territorial connection with the United States in that the prohibited transaction must have occurred on an American securities/financial market, or 'the securities market professional must be physically present in the US subsequent to his/her conviction in a foreign court.'³⁴⁷

³⁴⁵ Osode, *supra* note 82, at 262.

³⁴⁶ *Ibid.*

³⁴⁷ *Ibid.*

CHAPTER 10: CIVIL LIABILITY

As a result of insider trading being an extremely difficult crime to prove, providing for civil liability in addition to criminal liability has been thought as vital to an effective insider trading programme.³⁴⁸ 'The burden of proving a purely circumstantial case is less onerous in a civil case,'³⁴⁹ where guilt need only be shown on a balance of probabilities, rather than beyond a reasonable doubt as in criminal cases.

10.1 THE CIVIL REMEDY IN TERMS OF S 440F(4)

As mentioned above, a statutory civil remedy was first expressly provided for under s 440F(4),³⁵⁰ in terms of which, any person who contravened the insider trading provisions of s 440F(4)(a) was liable to any person for any loss or damage suffered by that person. The necessity of proving either intention or negligence was expressly excluded when dealings took place on a stock exchange or other financial market.³⁵¹ This exclusion arose as a result of the anonymity of stock-exchange dealings.³⁵² For statutory civil liability to arise the defendant must have contravened the criminal provisions of s 440F.³⁵³ As a result all the *essentialia* for the commission of the criminal offence must be met in order for civil liability to become a possibility.³⁵⁴ The claimant would then have to establish that loss or damage was suffered; and that the loss or damage was caused by the contravention of the criminal provisions, in other words that there

³⁴⁸ Newkirk & Robertson, *supra* note 223, at 9.

³⁴⁹ *Ibid.*

³⁵⁰ Of the 1973 Act (as inserted by the 1990 Act).

³⁵¹ Section 440F(4)(b) of the 1973 Act (as amended);

³⁵² Luiz, Stephanie M 'Prohibition against Trading on Inside Information – The Saga Continues' (1990) 2 *SA Merc LJ* 328 at 331.

³⁵³ Jooste, *supra* note 31, at 603.

³⁵⁴ *Ibid.*

was a causal link between the contravention and the loss or damage suffered.³⁵⁵ With the latter, the claimant did not have to prove, in the case of stock exchange dealings, 'that the defendant intended to cause damage or loss to him or that the defendant should as a reasonable man have foreseen that his dealing would cause loss to him.'³⁵⁶

As a result of the difficulty in identifying an individual victim of the insider,³⁵⁷ together with the fact that there is generally no causal link between the contravention and the loss or damage suffered, Jooste has described the civil remedy created by s 440F(4)(a) as 'an exercise in futility'.³⁵⁸ These aspects will be discussed in more detail below.

10.2 THE ABSENCE OF A DIRECT CAUSAL LINK AND AN IDENTIFIABLE VICTIM

A major problem in proving a civil case is the difficulty to empirically identify the harm of which insider trading is thought to cause.³⁵⁹ With face-to-face transactions, however, there may be some form of demonstrable harm as would be the case of a deliberate misrepresentation or inducement by the insider, which causes the other party (the outsider) to deal in the relevant securities.³⁶⁰ However, the majority of transactions occur not over the counter, but rather through anonymous stock exchanges where generally the outsider would have bought or sold shares irrespective of anything which the insider may have done and does so in full knowledge of the price of the securities with which they are dealing.³⁶¹ It is said that if an individual would have traded at the same price,

³⁵⁵ Jooste, *supra* note 31, at 603.

³⁵⁶ *Ibid.*

³⁵⁷ Hannigan, *supra* note 6, at 7.

³⁵⁸ Jooste, *supra* note 55, at 250.

³⁵⁹ Rider & Ashe, *supra* note 163, at 3.

³⁶⁰ Hannigan *supra* note 6, at 7.

³⁶¹ *Ibid* at 7-8.

whether or not there has been insider dealing, then there can be no connection between the insider dealing and the loss or damage suffered.³⁶² It has therefore been argued that in this situation, any loss or damage suffered by the individual transacting on a stock exchange is not caused by the insider dealing but rather 'by the initial non-disclosure of the information in question,'³⁶³ in other words, by the fact that the information has not been made public.³⁶⁴ Jooste presumes that the legislature intended that the loss or damage be the 'difference between the actual transaction price and what would have been that transaction price if the inside information had been made public.'³⁶⁵ This loss is said to 'occur regardless of whether insiders have dealt or not, for in any event the outsider would still have dealt and would have sustained the same losses.'³⁶⁶ It has therefore been argued that it is 'impossible to establish any relationship between the insider and the outsider other than the coincidental one of having both been in the market at the same time.'³⁶⁷ As a result, the civil remedy created by s 440F(4)(a) was futile as any action would fail for lack of a causal link between the criminal provisions of 440F and the loss or damage suffered.³⁶⁸

Even if one was to assume that a causal link referred to above does exist, there is still the problem of proving such a connection.³⁶⁹ It is argued that since an outsider is a willing buyer or seller he or she has not been misled and therefore cannot be said to be a victim.³⁷⁰ As a result, insider trading has been described as a victimless crime.³⁷¹ As majority of transactions occur through anonymous stock exchanges (as opposed to face to face transactions), it is 'very difficult, if not impossible, to link a buyer with a particular seller or link shares delivered

³⁶² Jooste , supra note 31, at 603.

³⁶³ Hannigan, supra note 6, at 8.

³⁶⁴ Jooste, supra note 31, at 603.

³⁶⁵ *Ibid.*

³⁶⁶ Hannigan, supra note 6, at 8.

³⁶⁷ *Ibid* at 7.

³⁶⁸ Jooste, supra note 31, at 603.

³⁶⁹ *Ibid*, at 604.

³⁷⁰ McVea, supra note 2, at 350.

³⁷¹ Hannigan, supra note 6, at 7.

with a particular sale.’³⁷² This has said to render proof of the causation requirement of s 440F(4) almost impossible.³⁷³ It has therefore been argued that, without being able to prove such a connecting link between the insider and the outsider, the outsider cannot really be seen as a victim of any potential crime committed by the insider.³⁷⁴

10.3 DISPENSING WITH THE NEED FOR PRIVACY AND THE EXISTENCE OF A CAUSAL LINK BETWEEN THE LOSS SUSTAINED AND THE DEFENDANT'S CONTRAVENTION

As has already been seen, the principle difficulty with a civil remedy is that it is difficult to show that a particular person made the loss represented by the insider's gain.³⁷⁵ America has responded to this problem by simply deleting any privacy requirement.³⁷⁶ The enactment of the Insider Trading Act, having followed the American approach, represented a change in emphasis in South African law regarding civil liability for insider trading as it indicated ‘a move away from the debate about the need to establish privacy between insider and outsider’ by similarly abolishing the causation requirement and adopting what has been called the ‘arbitrary’ approach.³⁷⁷ This same approach has been carried through into the Act. As will be seen, this represents a significant change in emphasis regarding the laws approach to the civil action from what was previously provided for under s 440F.³⁷⁸

³⁷² This is a result of brokers on the Johannesburg Stock Exchange operate a ‘clearing house’ for traded securities and therefore only deliver differences in balance to it (Jooste, supra note 55, at 250).

³⁷³ Jooste, supra note 31, at 604.

³⁷⁴ Brazier, supra note 7, at 3-20.

³⁷⁵ Douglas M Branson ‘Insider Dealing – Part III’ (1982) *Journal of Business Law* 536 at 536.

³⁷⁶ *Ibid.*

³⁷⁷ Jooste, supra note 89, at 456.

³⁷⁸ Of the 1973 Act (as amended).

10.4 WHO CAN CLAIM COMPENSATION IN TERMS OF THE ACT?

In terms of the Act, civil proceedings can be instituted by the Directorate of Market Abuse against inside dealers, 'encouragers' and 'disclosers'.³⁷⁹ The Directorate of Market Abuse sues on behalf of claimants for recovery of the 'profit made, or the profit that would have been made if the listed securities had been sold at any stage, or the loss avoided' by the inside dealer, plus a penalty imposed up to three times these profits or losses avoided.³⁸⁰ The amount recovered is paid into a specifically designated trust account, which is distributed amongst persons who dealt in the same securities at a certain time in relation to the insider dealing.³⁸¹

Section 77(8)(b) of the Act, provides for what has to be proved for a claimant to qualify as a proved claimant. There are two important observations regarding s 77(8)(b).³⁸² The first is that there is no requirement of privity between the insider and outsider.³⁸³ This means that in order to succeed with a civil action, a claimant does not 'have to show that the party with whom his/her transaction was consummated was the wrongdoer against whom the pecuniary awards contemplated under the Act have been made.'³⁸⁴ In other words, the Directorate

³⁷⁹ Section 83(1)(c) of the Act. This is the new name for the Insider Trading Directorate, which was established by the Insider Trading Act (s 12) as a committee of the Financial Services Board. The Insider Trading Directorate continues to exist but just under a new name (s 83(1)(a) and (b) of Act).

³⁸⁰ Section 77(7)(a) of the Act. In terms of this section, the amount recovered by the board as a result of the proceedings or as a result of an agreement of settlement must be deposited by the board directly into a specially designated trust account and- 'entitled to reimbursement of all expenses reasonably incurred by it in bringing such proceedings and in administering the distributions made to claimants in terms of subsection (8) and an additional sum equal to 10% of the gross amount so recovered less any amount of costs actually recovered from the other party prior to the finalisation of the distribution account', (b) the balance, if any, must be distributed by the claims officer to the claimants referred to in subsection (8) in accordance with subsection (9); (c) any amount not paid out in terms of paragraph (b) accrues to the board.'

³⁸¹ Section 77(7)(b) and 77(8)(b) of the Act.

³⁸² The same two observations apply to s 6(6) of the Insider Trading Act.

³⁸³ Osode, *supra* note 82, at 250.

³⁸⁴ *Ibid.* Osode is referring to the similar provision (s 6(6)) of the Insider Trading Act, which first abolished the requirement of privity in South Africa.

can now sue on behalf of a 'shareholder who sold when, having favourable news, insiders bought or the shareholder who bought when, having unfavourable news, insiders sold' without the need to show that insiders have bought or sold the plaintiff's shares.³⁸⁵ This has the effect of reducing the evidentiary burden that an aggrieved investor is said to bear when seeking compensation.³⁸⁶ The second observation is that there is no requirement that the claimant prove actual loss.³⁸⁷ According to Osode, 'it appears that financial injury deserving of some compensation is said to be irrevocably presumed wherever a claimant is able to bring him/herself within the said provisions.'³⁸⁸

In terms of s 77(8)(b)(i) of the Act,³⁸⁹ claimants are required to prove, in addition to the fact that they were affected by the dealings referred to in subsecs (1) to (4),³⁹⁰ that they also dealt around the same time as the insider.³⁹¹ Whether a

³⁸⁵ Branson, *supra* note 375, at 536. The explanation provided by Branson has been used to show the position in South African law.

³⁸⁶ *Ibid.*

³⁸⁷ *Ibid.*

³⁸⁸ *Ibid.*

³⁸⁹ Section 6(6)(a) of the Insider Trading Act required claimants to prove that they were affected by the dealings referred to in subsection (1) and that-

'(a) in the case where the inside information was made public within a week after the individual referred to in subsection (1) dealt, they dealt in the same securities or financial instruments at any time after the individual referred to in subsection (1) so dealt and before the inside information was made public;

(b) in every other case, they dealt in the same securities or financial instruments on the same day as the individual referred to in subsection (1).'

³⁹⁰ Section 77(1) provides: 'An insider who knows that he or she has inside information and who-

(a) deals directly or indirectly or through an agent, for his or her own account in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it; at any stage, or avoids a loss, through such dealing; and

(b) makes a profit or would have made a profit if he or she had sold the securities at any stage, or avoids a loss, through such dealing; and

(c) fails to prove, on a balance of probabilities, any one of the defences set out in section 73(1)(b) is liable, at the suit of the board in any court of competent jurisdiction, to pay to the board-

(i) the equivalent of the profit or loss referred to in paragraph (b);

(ii) a penalty, for compensatory and punitive purposes, in a sum determined in the discretion of the court but not exceeding three times the amount referred to in paragraph (i);

(iii) interest; and

(iv) costs of suit on such scale as may be determined by the court.'

Section 77(2) provides: 'An insider who knows that he or she has inside information and who-

(a) deals, directly or indirectly, for any other person in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it;

claimant will be considered to be a proved claimant depends on the time lapse between insider dealer's dealing and the publication of the inside information.³⁹²

If the time lapse was five days or less then the claimant will qualify as a proved claimant if he can in addition prove that he dealt in the same securities after the

(b) makes a profit for that other person or would have made a profit if the securities had been sold at any stage, or avoids a loss, through such dealing; and

(c) fails to prove any one of the defences set out in section 73(2)(b) on a balance of probabilities, is, subject to subsection (3), liable, at the suit of the board in any court of competent jurisdiction, to pay to the board-

(i) the equivalent of the profit or loss referred to in paragraph (b);

(ii) a penalty, for compensatory and punitive purposes, in a sum determined in the discretion of the court but not exceeding three times the amount referred to in paragraph (i);

(iii) interest;

(iv) the commission or consideration received for such dealing; and

(v) cost of suit on such scale as may be determined by the court.'

Section 77(3) provides: 'An insider who knows that he or she has inside information and who-

(a) discloses the inside information to any other person; and

(b) fails to prove on a balance of probabilities the defence set out in section is, subject to subsection (5), liable, at the suit of the board in any court of competent jurisdiction, to pay to the board-

(i) if the other person dealt in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it, the equivalent of the profit which the person made or would have made if the securities had been sold at any stage, or the equivalent of the loss avoided, as a result of such dealing;

(ii) a penalty, for compensatory and punitive purposes, in a sum determined in the discretion of the court but not exceeding three times the amount referred to in paragraph (i);

(iii) interest;

(iv) the commission or consideration received for such disclosure; and (v) cost of suit on such scale as may be determined by the court.'

Subsection (4) provides: 'An insider who knows that he or she has inside information and who encourages or causes any other person to deal in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it is, subject to subsection (3), liable, at the suit of the board in any court of competent jurisdiction, to pay to the board-

(a) if the other person dealt in such securities, the equivalent of the profit which the person made or would have made if the securities had been sold at any stage, or the equivalent of the loss avoided, as a result of such dealing;

(b) a penalty, for compensatory and punitive purposes, in a sum determined in the discretion of the court but not exceeding three times the amount referred to in paragraph (a)

(c) interest;

(d) the commission or consideration received for such encouragement; and

(e) cost of suit on such scale as may be determined by the court.'

³⁹¹ In terms of s 77(8)(b) of the Act, the claimants wanting to institute a civil action must prove that, '(i) they were affected by the dealings referred to in subsections (1) to (4); and (ii) in the case where the inside information was made public within five trading days from the time the insider referred to in subsections (1) and (2), or the other person referred to in subsections (3) and (4) dealt, they dealt in the same securities at the same time or any time after the insider or other person so dealt and before the inside information was made public; or (iii) in every other case, they dealt in the same securities at the same time or any time thereafter on the same day, as the insider or other person referred to in subparagraph (ii).'

³⁹² Jooste, *supra* note 44, at 301.

insider dealer dealt and before publication of the inside information.³⁹³ If the time lapse was more than 5 days, he will have to prove that he dealt on the same day as the insider dealer dealt.³⁹⁴ From the above it can therefore be seen that the legislative approach in regard to the civil remedy, in both the Insider Trading Act and the Act, has been to move 'away from requiring a direct causal link between the insider dealing and the claimant's loss to the chosen approach of disregarding causation and compensating claimants who dealt around the same time as the insider dealer.'³⁹⁵

'If insider trading is to constitute a wrong to persons with whom an insider trades, this must be because the insider has a duty to disclose the inside information to them.'³⁹⁶ Such a duty can arise from, for example, a fiduciary relationship existing between the insider and those persons.³⁹⁷ An insider does not ordinarily owe a duty to disclose the inside information to the claimants who dealt around the same time as him. Therefore, an important theme underlying the civil provisions of the Act relates to the reasoning as to why it is those claimants who dealt around the same time as the insider dealer that should be awarded civilly. In terms of the surrogate plaintiff theory, the insider is deemed to owe a duty of disclosure to contemporaneous traders (traders who traded in the same time period and in the same class of shares as the insider), for any transactions undertaken on the basis of inside information in the relevant shares or securities.³⁹⁸ The theory presupposes that since the information is material, these investors would have relied on it and would have altered their conduct accordingly had the information been disclosed.³⁹⁹ The insider is then deemed to have breached this duty by trading on the inside information.⁴⁰⁰ The casual

³⁹³ Section 77(8)(b)(ii) of the Act.

³⁹⁴ *Ibid.*

³⁹⁵ Jooste, *supra* note 44, at 301.

³⁹⁶ Blackman *et al*, *supra* note 1, at 5-376.

³⁹⁷ *Ibid.*

³⁹⁸ McVea, *supra* note 2, at 352.

³⁹⁹ Jooste, *supra* note 89, at 457.

⁴⁰⁰ McVea, *supra* note 2, at 352.

link between the insider's wrongful act of trading and the injured party's loss is presumed and the loss is deemed sufficiently proximate so as to remove the need for privity.⁴⁰¹ One of the justifications for the abolition of the need for privity is that 'the contemporaneous traders are "surrogate plaintiffs" for those who actually were in privity with the insider.'⁴⁰² It is thought that surrogate plaintiffs are necessary to fulfil the deterrent purposes of anti-insider trading legislation.⁴⁰³ This is the approach that has been taken in the American legislation and has been adopted into South African law.

The inclusion of contemporaneous traders as potential claimants may lead to liability astoundingly out of proportion to any gain the insider could have made as a result of a duty owed to all such traders.⁴⁰⁴ However, draconian liability can be averted by limiting the damages payable by the defendant.⁴⁰⁵ The approach is also considered to be artificial and that it leads to fortuitous plaintiffs, who would have bought or sold shares anyway, recovers a windfall.⁴⁰⁶ However, fortuitous plaintiff's and windfall recoveries, which are not as a general rule to be encouraged, are thought to be justifiable when the primary purpose is not compensation but to further the socially beneficial goal of deterrence of insider dealing.⁴⁰⁷

As already discussed, under both the Insider Trading Act and the Act, having adopted the same approach, it is not longer necessary to establish a 'direct causal link between the insider dealing and the claimant's loss'.⁴⁰⁸ This is as a result of the abolition of the privity requirement. The fact that there does not need to be any connection between the insider and outsider other than the basis

⁴⁰¹ McVea, *supra* note 2, at 352

⁴⁰² *Ibid* at 353.

⁴⁰³ *Ibid*.

⁴⁰⁴ Branson, *supra* note 375, at 537.

⁴⁰⁵ McVea, *supra* note 2, at 353.

⁴⁰⁶ Jooste, *supra* note 31, at 605.

⁴⁰⁷ McVea, *supra* note 2, at 353.

⁴⁰⁸ Jooste, *supra* note 89, at 456.

that they were trading in the same time period can be seen to be one of the important themes underlying the civil provisions of the Act. This approach is also aimed at the protection of the integrity of the market as reducing the evidentiary burden should in turn facilitate successful reliance on the relevant statutory provisions which should increase investor confidence in the integrity of South Africa's financial markets.⁴⁰⁹ This is indicative of change of emphasis from that of s 440F(4)(a), which required the claimant to prove the existence of a causal link between the insiders dealing and the loss or damage suffered.

The fact that a claimant is not required to prove actual loss is another important theme. Claimants who dealt around the same time as the insider dealer are presumed to have suffered financial injury deserving of some compensation. As stated above, in terms of the surrogate plaintiff theory, insiders are deemed to owe a duty of disclosure to contemporaneous traders for any transactions undertaken on the basis of inside information in the relevant shares or securities. This seems to highlight the insider's non-disclosure of inside information as the harm that anti-insider trading legislation seeks to prevent. Investors who traded at the appropriate time in the same class of shares as the insider were at an informational disadvantage compared to that of the insider and therefore the insider committed a wrong against those persons by not disclosing the information. Section 440F seemed to be more focused on the effect of the insider trading rather than the unreasonable non-disclosure of the inside information that causes the injury. It is submitted that a further change of emphasis represented in the Act, is the recognition of the fact that any loss or damage suffered by an individual transacting on a stock exchange is a result of the non-disclosure of the inside information rather than the insider dealing. Although the Act does not provide an express duty on companies to disclose inside information, it seems to be implied provided for when one looks at the rationale behind the civil remedy.

⁴⁰⁹ Osode, *supra* note 82, at 250.

It is thought that a civil remedy, as provided for in the Act, may provide a symbolic function as its existence could serve to further the goal of investor confidence.⁴¹⁰ The provisions also seem to focus on a deterrence effect, discouraging unreasonable non-disclosure of information and thereby promote public confidence in capital markets integrity. The deterrence effect stems from the fact the inclusion of contemporaneous traders as potential claimants may lead to liability astoundingly out of proportion to any gain the insider could have made as a result of a duty owed to all such traders.

The legislature in adopting this approach seems to be again focused on the effect of deterrence, punishment and protection of the integrity of the market. The general approach underlying the civil provisions in particular is the fact that unless one discloses the inside information one is not allowed to deal.

10.5 NO CIVIL LIABILITY FOR ‘DISCOURAGING’

The Act, as did the Insider Trading Act, excludes the ‘discouraging’ offence from the ambit of civil liability and as such an insider will not incur civil liability for discouraging or stopping a person from dealing.⁴¹¹ This exclusion has been criticised on the basis that discouragement’ is seen as just ‘as harmful as ‘encouraging’ or ‘disclosing’ and that it should therefore have the same consequences.⁴¹²

⁴¹⁰ McVea, *supra* note 2, at 351.

⁴¹¹ Jooste, *supra* note 89, at 455.

⁴¹² *Ibid.*

CHAPTER 11: SUMMARY AND CONCLUDING COMMENTS

From the previous discussions, it can be seen that there are various common themes that run through South Africa's past and present insider trading laws, representing consistencies as well as changes in emphasis as to what has been considered to be the 'wrong' of insider trading. It was shown that an important theme of the Act is the fact that in order for a transaction to be brought within its purview, the accused must be an 'insider' and the transaction must involve the use or disclosure of or reliance on data that qualifies as 'inside information'.⁴¹³ The policy objective of deterrence, for example, was another one of these overarching themes of the Act, indicating a harsher line taken by the legislature. The focus on deterrence was thought to be in contrast to the legislature's original focus with s 233, where the emphasis seemed to be focused solely on the criminalising of insider trading.

It was further shown that a trend in South Africa's insider trading laws has been to broaden the definition of an 'insider' as well as that of 'inside information', the justification of which having shifted more towards the rationales of market fairness, integrity and efficiency. As opposed to classic insider dealing merely involving 'dealing' by an insider, the offences of 'encouraging' or 'discouraging' and 'disclosure' are in addition included within the purview of the Act, representing the more modern objective of insider trading legislation, prohibiting not just insider trading *per se* but also related conduct. The broad range of offences represents a significant extension of liability from the previous position under s 233 and s 440F and is also an indication that the legislature considers the conduct of aiding and abetting to be a 'wrong' worthy of being punished. Despite the above, it was submitted that there is some conduct worthy of punishment that has been excluded from the scope of the Act, for example, the fact that abstaining from dealing on the basis of inside information has never

⁴¹³ Osode, *supra* note 82, at 243.

been an actionable offence. The underlying rationales of market fairness, integrity and efficiency were also seen in the civil context, where as a result of there being no real quantifiable loss or damage that can be attributed to any one 'victim', it was submitted that there has been a change in emphasis from viewing insider trading as a 'wrong' which causes harm to an individual investor, to one that affects everyone in the market who dealt around the same time as the insider dealer. In terms of this approach, it is the market which is harmed as a result of the insider's non-disclosure of the inside information rather than the actual dealing itself.

A further central theme was the lack of connections or links required in order to be found criminally or civilly liable under the Act. The Act's 'by virtue' and 'tippee' categories of 'insider' were shown to be illustrative of this, both of which render it unnecessary to establish any causal or connecting link between a person and an issuer of securities in order to fall within the purview of the Act. This lack of connectivity was also illustrated by the fact that no territorial connection is required between any element of the offences or civil wrongs and South Africa. This was also the case with the civil provisions, there being no need to establish privity between the insider and outsider nor actual loss suffered by the claimant. Lastly, for information to be considered 'inside information', it is not necessary that such information relates to the internal affairs of the company but may relate to the market information generally. However, despite this lack of connectivity, it is concluded that as a result of the Act still requiring an accused to be either be an 'insider' to or have received the 'inside information' from an 'insider', there is still a link between the Act and s 233, despite the Act's emphasis on the possession of 'inside information'.

Finally, it was also shown that, contrary to the previous position under s 233, the Act does not require an accused to have dealt on the basis of the inside information or to have received a benefit in any way in order to have committed

an offence.⁴¹⁴ It was thought that the legislatures motive behind dispensing with these requirements was due to the evidential difficulties in securing a successful prosecution for insider trading as opposed to representing any real change in emphasis as to what the law has regarded as the 'wrong' of insider trading.

⁴¹⁴ As was discussed, this position is different in regard to civil liability.

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