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CLIENT UPDATE: THE INS AND OUTS OF INSIDER TRADING

(PART 1 OF 2)

ASIC's recent announcement that a technology systems upgrade will enable it to watch and tag trades by individual investors¹ is a timely reminder that companies and persons in possession of "*inside information*" need to be aware of the law governing its use and disclosure.

This client update:

- briefly describes the general offence / what constitutes prohibited conduct; and
- highlights the extent of ASIC's recent activity in prosecuting insider trading and market misconduct offences.

A separate article providing companies with practical guidance on managing risk in this area will follow.

WHAT IS "INSIDE INFORMATION"?

Broadly, "*inside information*" refers to "*information*" that is not "*generally available*", and if it were "*generally available*", a reasonable person would expect it to have a material effect on the price or value of particular listed securities or other financial products. It does not matter if the information is false.

What amounts to "*information*" is very broad, and includes matters of supposition, other matters that are not sufficiently certain to justify public disclosure, and matters relating to the intentions, or likely intentions, of a person.

Such "*information*" will be "*generally available*" if it:

- consists of "*readily observable matter*"² (i.e. it is plainly apparent to anyone minded to look);

¹ Australian Financial Review, "ASIC turns eye to insider trading", Matthew Drummond, 25 November 2013; "Insider traders under a brighter spotlight", Tony Boyd, 29 October 2013

- has been made known in a manner that would (or would be likely to) bring it to the attention of persons who commonly invest / trade in shares and a reasonable period for it to be disseminated has elapsed; or
- it consists of deductions, conclusions or inferences made or drawn from such readily observable matter or previously disclosed information.

In short, there is a broad class of information that could potentially constitute "inside information" for the purposes of the prohibition. As a consequence, listed entities (and intermediaries / advisors etc. dealing with those entities who may obtain inside information) need to:

- have strong governance protocols / policies / procedures in place regarding the use and disclosure of "inside information"; and
- educate officers and employees regarding:
 - the practical application of the insider trading and market misconduct provisions of the Corporations Act; and
 - the importance of compliance with governance protocols / policies / procedures regarding use, handling and disclosure of "inside information".

WHAT IS THE PROHIBITED CONDUCT?

In summary, the "insider trading" provisions in the Corporations Act prohibit:

- the direct or indirect acquisition or disposal of "Division 3 financial products"³ while in possession of "inside information";
- the procurement of another person to acquire or dispose of such financial products while in possession of "inside information"; and
- the communication of "inside information" to another person for the purpose of the other person acquiring or disposing of such financial products.

Where a contravention occurs, the potential individual penalties are significant.⁴

RECENT ASIC SUCCESS

Since assuming responsibility (from ASX) for the supervision of trading on Australia's domestic licensed equity, derivatives and futures markets, ASIC has been active in its prosecution of the insider trading and market misconduct⁵ offences. Recent announcements include:

Date of ASIC announcement	Parties involved	Conduct	Penalty
26 November 2013	CEO	Communicating inside information about a pending takeover to an associate, along with money and instructions to purchase shares in the target.	Awaiting sentence.
23 August 2013	Chairman	Placed orders to sell more than 3.4 million shares while in possession of inside information relating to the financial performance of a listed company. This trading was prior to the release of half year results, and following	Fined \$50,000 and automatically disqualified from managing corporations for five years.

² It does not matter how many people actually observe the relevant information, nor does it matter if there is a delay between when the information becomes readily observable and when it is in fact observed. Information may be readily observable even if no one observed it.

³ Meaning securities, derivatives, interests in a managed investment scheme and other financial products that are able to be traded on a financial market.

⁴ Up to 10 years imprisonment and / or a fine of the greater of \$4,950,000 or three times the value of any benefit derived from the contravention.

⁵ Since 1 January 2009, ASIC has prosecuted 31 insider trading actions.

Date of ASIC announcement	Parties involved	Conduct	Penalty
		the release of those results, the share price of the relevant company fell substantially.	
8 August 2013	Investment banking associate	Communication of inside information regarding pending takeover announcements knowing that associates would be likely to trade on the information.	23 months jail.
15 February 2013	Investment bank executive and company vice president ⁶	The acquisition of inside information relating to proposed takeovers, and the procurement of one or more persons to acquire financial products relating to the proposed target companies.	2 years and 3 months jail, to serve a minimum term of 15 months. In making the order, the judge took into consideration the early guilty plea and high level of cooperation with ASIC's investigation.
19 December 2012	Executive vice president with international energy company	Purchase of shares in two listed companies while in possession of inside information (relating to employer's interest in those companies) at the time the shares were purchased.	Two years imprisonment (with at least 12 months served before being eligible for parole), a pecuniary penalty order in the amount of \$640,857.18 ⁷ and disqualification from managing a corporation in Australia, including acting as director of a company, for a period of five years from the date of release from prison.

CONCLUSION

ASIC:

- has recently completed a technology upgrade that will enable it to target individual trading activity;
- has been successful in its pursuit of insider trading and market misconduct offences; and
- will, given its core function of promoting confident and informed participation by investors and consumers in the financial system, continue to pursue possible contraventions and questionable conduct with vigour.

Accordingly, the need for appropriate governance protocols / policies / procedures and education for officers and employees regarding the practical application of the insider trading and market misconduct provisions of the Corporations Act is clear.

DLA Piper Australia can assist clients by advising on the scope of the prohibition (including the statutory defences), the establishment of governance protocols, training programs and providing guidance in the event of ASIC investigations.

⁶ The charges related to conduct engaged in while working for three different employers.

⁷ This resulted from separate proceedings conducted by the Australian Federal Police under the *Proceeds of Crime Act 2002*.

MORE INFORMATION

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