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LEGAL FRAMEWORK FOR INSIDER DEALING UNDER THE NIGERIAN LAW

1. Introduction

It is undeniable that exploiting information that is inaccessible to the other party has been a longstanding facet of human behaviour. It is inherent in human nature to prioritise safeguarding one's interests. Consequently, the issue of insiders misusing information obtained through their special relationship with a company is far from new. However, opinions diverge on whether insiders who engage in securities transactions of the issuer, leveraging this privileged access to information, should be held accountable. Some argue that the acquisition of superior information should not only be condoned but also exempt from penalties. As a result, the regulation of insider dealing presents and will likely continue to present a multitude of challenges. The intricacies of the financial landscape in which legal and regulatory frameworks operate amplify the practical and legal hurdles faced by those tasked with enforcing and interpreting the law. It is against this backdrop that a thorough examination of the concept of insider dealing under Nigerian law becomes imperative.

2. An Insight on The Keywords "Insider" And "Insider Dealings"

The Black's Law Dictionary defines an insider as someone who has knowledge of information not available to the general public.[2] Section 315 of the Investment and Securities Act (ISA) defines an insider as any person who is connected with the company in one or more of the following capacities:

2.1 a director of the company or a related company;

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2 *Black's law Dictionary* (9th edn) Thomas West Publishing, para 866, p. 1142.

2.2 an officer of the company or a related company;

2.3 an employer of the company or a related company;

2.4 an employee of the company, involved in a professional or business relationship of the company;

2.5 any shareholder of the company who owns 5 per cent or more of any class of securities or any person who is or can be deemed to have any relationship with the company or member;

2.6 members of the audit committee of a company.[3]

Insider dealing occurs when an individual possessing information that significantly impacts a company's stock value engages in the buying or selling of securities related to that company, thereby securing more favourable terms in the transaction than would have been the case had the other party been privy to the same information. This affords the insider the opportunity to either yield a profit or avert a potential loss, contingent on whether the information, once made public, will cause the share price to rise or fall."[4]

According to Black's Law Dictionary, insider trading is articulated as the utilisation of substantial, non-public information in the trading of a company's shares by a corporate insider or any other individual who bears a fiduciary responsibility to the company. This definition underscores the ethical and legal ramifications tied to such actions.[5]

3. Laws Regulating Insider Dealing in Nigeria

- The Nigerian Investments and Securities Act
- Nigeria Stock Exchange[6]
- Nigerian Code of Corporate Governance[7]

3.1 The Investments and Securities Act

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3 Investment and Securities Act 2007, section 315.

4 Gower and Davies, *Principles of Modern Company Law,* (8th edn, Sweet & Maxwell, London, 2008) 1083-1084.

5 *Black's law Dictionary* (9th edn) para 866, p. 1142.

6 The Nigerian Stock Exchange is now referred to as the Nigerian Exchange Group (NGX Group).

7 Nigerian Code of Corporate Governance 2018, available at <https://pwcnigeria.typepad.com/files/nigerian-code-of-corporate-governance-2018-1.pdf> accessed 14 October 2024.

Section 111 of Investments and Securities Act ("ISA"), prohibits any person who is an insider of a company from buying, selling or otherwise dealing in the securities of a company which are offered to the public for sale or subscription if he has information which he knows is unpublished price sensitive information in relation to those securities.[8] The Act therefore prohibits insider dealing which it defines as where a person who, having some confidential and price sensitive information not generally available to the public, utilises such information to buy or sell securities for the benefit of himself. The definition of an ''insider'' under the statutory regulation encompasses persons who are or can be deemed to have any connection with the company or a member of the company, including persons who, in their professional capacity, obtained unpublished price sensitive information in relation to the securities of the company.[9]

Upon consideration of the above cited section 111(1) of the ISA, it may be right to conclude that for any person to contravene that provision, the following conditions must be met:

3.1.1 the person in question must be an insider of a company;

3.1.2 the insider must have bought, sold and otherwise dealt in the securities of the company which are offered to the public for sale or subscription;

3.1.3 the insider must have had information which he knew was unpublished price-sensitive information in relation to those securities which he bought, sold or otherwise dealt in, offered either to the public for sale or subscription.[10]

Notably, it has been argued elsewhere that the two essential elements that make up a dealing offence are:

(a) that an individual must have information as an insider; and

(b) that the insider must deal in securities that are price-affected securities in relation to the information – the test is that the prices of price-affected securities will likely be significantly affected if information related to such securities is made public.

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8 Investments and Securities Act 2007, section 111.

9 Securities and Exchange Commission Rules 2013, Rule 400.

10 In putting this more succinctly, Orojo posits that where a director of a company who is aware that a company is crashing due to some unsuccessful business risks sells his shares, knowing full well that the decision of the board to cut the dividend will be announced in few days, is guilty of insider dealing. See, J. O. Orojo, *Company Law and Practice in Nigeria*, 5th edn (South Africa: LexisNexis Butterworths) 390.

Nevertheless, it is crucial to note that section 315 of the ISA provides a comprehensive definition of "insider dealing," which encompasses not only insider trading but also instances where an individual or a group, possessing confidential and price-sensitive information not readily available to the public, leverages such information for the purpose of buying or selling securities, whether for their benefit or for that of others. At this juncture, it is apt to assert that a meticulous examination of the definitions of "an insider" and "insider dealing" reflects a deliberate intent on the part of the drafters to encompass any conceivable scenario wherein an individual, by virtue of their position or their affiliation with either the company or one of its members, gains access to information they are cognizant constitutes unpublished, price-sensitive information regarding the securities of the company offered to the public for sale or subscription. In such cases, should they opt to utilize this information, it is incumbent upon regulatory authorities and market participants to ensure that the highest standards of integrity and compliance are upheld, safeguarding the integrity and transparency of the financial markets.[11]

3.2 Nigerian Stock Exchange

The Nigerian Stock Exchange was founded in 1961 in Lagos.[12] The Nigerian Stock Exchange Rulebook gives the definition of “inside information” to mean information related to an issuer of a security or the issuer’s securities, either directly or indirectly, which has not been published and whose disclosure may have a significant effect on the price of securities and stocks so listed and traded or derivative instruments which are linked to those securities.[13]

The portfolio of stocks bought by corporate insiders typically outperforms the stocks selected on non-privy information by a regular investor.[14] Moreover, the distributions which are made by “knowledgeable” sellers have, most of the time, come before substantial price declines. At the core of the insider trading debate is the crucial question of whether or not it should be ruled as an offence, and whether it is good for the financial markets. In 1934, the United States Congress decided that it was a danger to the economy and in response to this decision the Securities and Exchange Commission (SEC) has since regulated the practice of insider trading in the United

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11 Investment and Securities Act 2007, section 315.

12 Nigeria Exchange Group available at <https://en.wikipedia.org/wiki/Nigerian_Exchange_Group > accessed 14 October 2024.

13 Nigerian Stock Exchange Rulebook, Rule 17(3).

14 Seyhun Nejat, “Insiders Profits, Cost of Trading, and Market Efficiency” (2015) 16 *Journal of FinancialEconomics,*<https://pdfs.semanticscholar.org/0075/002ae61bb50d7567582f1bbc647cd770d36b.pdf.> accessed 14 October 2024.

States.[15] In Nigeria, however, it was not until 1990 that insider trading was strictly regarded as an offence after a written recommendation presented by the Nigerian Law Reform Commission (NLRC).[16]

The justification or otherwise of insider trading has been discussed on two levels:

One: is it just and fair to have trading on largely different levels of individual information and understanding?

Two: is it an economically sound policy to allow the practice of insider trading without sanction?

It is however, important to note that the United States of America was the first, and for quite a while afterwards, the only country to proscribe the act of making trading decisions on sensitive non-public information as illegal.

3.3 Nigerian Code of Corporate Governance

Corporate governance refers to the principles and procedures enunciated in the UK Cadbury Report 1992 and the Organization for Economic Co-operation and Development (OECD) Principles of Corporate Governance 1999. Within the general Principles in these documents, the company is required to recognize that it has legal, contractual, social, and market-driven obligations to not only its shareholders, but also to non-shareholders and stakeholders such as employees, investors, creditors, customers, suppliers, local communities, customers, and policy makers. But the rights of shareholders need to be respected, and they should be assisted to exercise those rights and be treated equitably through open and effective communication of information, and encouraged to participate in the company's general meetings.[17]

The company loses a lot when insider dealing is a profitable business practice engaged in by the directors. The corporate reputation of the company is tarnished, investors' confidence eroded and prospects for access to capital dimmed, with the consequence of a fall in liquidity and a decrease in market efficiency. Insider dealing can also result in litigation against the company and the directors with possible civil penalties and criminal sanctions or prosecutions. Where its impact on the company's share price is significant it may lead to class actions, and if the conduct of the

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15 *Peek v Gurney* (1873) L.R. 6 HL 377.
16 Nigerian Law Reform Commission Act (Laws of the Federation of Nigeria 2004), Cap. N118.
17 Organization for Cooperation and Development Principles of Corporate Governance, 1990, Article IV.

directors is in breach of their fiduciary duties, they can be held liable in their capacity as directors.[18]

To prevent insider dealing, relevant statutory regulations and the company's internal policies need to be fully understood, upheld and applied in the management and operations of the company.

Implementation of the principles of corporate governance within the company introduces a culture of adherence to ethics and code of conduct for the board of directors, chief executive officers, accounting officers and auditors. Since access to the company's confidential information underlies insider dealing, the board, in particular, bears the ultimate responsibility to drive and monitor the flow of such information within the company. The board also needs to determine the process of flow of share price-sensitive information to the shareholders and the investing public in a timely and transparent manner to avoid information asymmetry which breeds insider dealing. Board oversight of executive directors and management has been identified as a key principle of corporate governance towards ensuring transparency and accountability in the business and affairs of the company.[19] Therefore, the board must implement an effective system of oversight of the processes for information flow within and through the company before announcement or publication to the public. The implication of informational hierarchy requires probative inquiries to determine the effectiveness of processes and procedures for directorial supervision of employees in high-risk points of the information flow-chart of the company. Regular reviews of the processes and procedures are necessary to ascertain the levels to which the code of conduct has been voluntarily imbibed and practised by employees across the company's hierarchy.[20]

In Nigeria, the current Code of Corporate Governance 2018 recommends the approach of ''apply and explain'', a variant of the UK ''comply or explain". Under the Nigerian approach, the companies and directors are required to adopt ethical practices, and the principles contained in the Code or to explain the application if different from the stipulated mode. Directors are charged with the responsibility of explaining how the company's operations apply the content of the Code towards

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18 Babajide Shoroye, 'Insider Dealing and Corporate Governance: Understanding the Legal Position of Directors' (2022) available at < https://www.ajol.info/index.php/naujilj/article/view/225875> accessed 14 October 2024.

19 Brian Ikol, 'An Analysis of the View that the Corporate Governance Systems Worldwide are Inevitably Converging Towards a Model Based on Shareholder Primacy and Dispersed Ownership Structure' (2012) available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2049764> accessed 14 October 2024.

20 Ibid.

achieving transparency and accountability in protecting the broad interests of shareholders and other stakeholders such as the employees, creditors and the larger society.

A common underpinning of the approach in both the UK and Nigeria is that, unlike statutory regulations where compliance is mandatory and non-compliance is visited with civil or penal sanctions, the company and management are expected to voluntarily imbibe the corporate culture of fairness, transparency and accountability. Thus, under corporate governance, the approach towards curbing insider dealing allows for flexibility of the board and management to determine how best to achieve best practices in line with cultivated corporate culture of ethics, values and integrity. Directors may choose to comply with the prescribed principles of corporate governance or apply such principles in ways different from the stipulated mode, provided that the intended outcome as envisaged under the principles is achieved.

It has been noted that good corporate governance is ultimately measured by the quality of the individuals involved, and their ability to take collective action and achieve a desired result, despite often different and conflicting interests, in a way that is appropriate to the regulatory and market environment, including the culture of norms and values of the company. Like insider dealing, directors are key to the practice of corporate governance. As an agency problem, their position and status in the company expose them to the practice of insider dealing. However, it is yet to be clear how, as individuals, they can play a decisive role in preventing insider dealing through corporate governance. What is clear, however, is that their role is indispensable in the implementation of the principles of corporate governance towards the prevention of insider dealing.[21]

4. Penalties For Insider Dealing Under the Nigerian Law

- Civil Penalties
- Criminal Penalties

4.1 Civil Penalties

In furtherance of the powers under Section 116 (1) ISA, the SEC or the Investments and Securities Tribunal (IST) can order a person who is liable for insider dealing (trading) to pay compensation, as the case may be, to any aggrieved person who, in a transaction for the purchase or sale of securities entered into with the first-

[21] Babajide Shoroye, 'Insider Dealing and Corporate Governance: Understanding the Legal Position of Directors' (2022) available at <https://www.ajol.info/index.php/naujilj/article/view/225875> accessed 14 October 2024.

mentioned person or with a person acting for or on his behalf, suffers a loss because of the difference between the price at which the securities would have likely been dealt in such a transaction at the time when the first-mentioned transaction took place, if the contravention had not occurred. It should be noted that the amount of compensation for which a person is liable is the amount of the loss sustained by the person claiming the compensation or any other amount as may be determined by the SEC or the IST. However, by section 114 of the ISA, any transaction done in contravention of sections 112 and 111 of the ISA[22] is voidable at the instance of the SEC.

As for the punishment for the breach of any provision of the Amendments to the NSE Rulebook, it is worth noting that the NSE may suspend trading in an instrument with effect from such time as it may determine if there are reasonable grounds to suspect the Issuer failed to comply with disclosure rules as stipulated under the NSE Rulebook.[23] The NSE may further impose such conditions on the procedure for lifting the suspension as it considers appropriate. [24]

Rule 198 of the SEC Rules 2013 also supports the powers of the NSE to suspend from trading, a security listed on the NSE. The Rule, however, imposes a duty on the NSE to notify the SEC within 24 hours of any such suspension, stating the effective date and the reasons for the suspension. However, the SEC Rules allow the issuer of a suspended security to appeal to the SEC for a review.[25] In the same vein, Rule 202 of the SEC Rules 2013[26] allows any company, enterprise, registrar, issuing house, stockbroker, dealer or any other person or institution engaged or involved in the issuing, sale buying or other trading in securities of companies to apply to the SEC for a review. This right of review extends to enterprises covered by the ISA and the SEC Rules directly affected by any direction or decision made under any bye-law, rule or regulation of an exchange or any other Self-Regulatory Organization.

Relatedly, the SEC is empowered under Rule 601 of the SEC Rules 2013[27] to determine the quantum of compensation for insider dealing cases.

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22 Investment and Securities Act 2007, sections 112 and 111.
23 Nigerian Stock Exchange Rulebook, Rule 21.
24 Ibid, Rule 21.
25 Securities and Exchange Commission Rules and Regulations, 2013, Rule 198(3).
26 Ibid, Rule 202.
27 Ibid, Rule 601.

4.2 Criminal Penalties

By section 115 ISA, any person who engages in insider dealing commits an offence and is liable on conviction – in the case of a person not being a body corporate, to a fine of not less than N500,000 or an amount equivalent to double the amount of profit derived by him or loss averted by the use of the information obtained in contravention of any of the provisions of this part. A guilty party may alternatively be liable to imprisonment for a term not exceeding seven years; or in the case of a person being a body corporate, to a fine not less than N1,000,000 or an amount equivalent to twice the amount of profit derived by it or loss averted by the use of the information obtained in contravention of any of the provisions relating to insider dealing.[28]

However, given the requirement of proof beyond reasonable doubt in criminal cases,[29] it is often difficult to prosecute persons for insider dealing. As noted by a commentator, the difficulty with prosecution in insider dealing cases often arises because of the paucity of direct evidence and reliance on circumstantial evidence, which often prove to be inadequate to ground a conviction for a crime of this nature.[30] In this wise, it is believed that Nigeria can benefit from two United States (US) Court decisions involving **United States v Gamache**[31] **and SEC v Sargent**[32] where the US Courts upheld convictions based on cogent and compelling circumstantial evidence, the same having met the threshold of admissibility. As a matter of fact, it is equally trite under Nigerian law that relevance is the main requirement for the admissibility of any evidence under the law of evidence.[33]

5. Conclusion

The practice of insider trading, the unethical exploitation of non-public information for personal gain, poses a significant threat to the integrity of financial markets. This insidious activity undermines investor confidence, distorts market prices, and erodes the foundation of fair and transparent commerce. In Nigeria, the prevalence of insider trading has cast a shadow over the capital market, hindering its growth and deterring potential investors. To address this pressing issue and safeguard the interests of all market participants, a comprehensive and proactive approach is essential. While Nigeria has enacted laws prohibiting insider trading, the existing regulatory

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28 Investment and Securities Act 2007, section 115.
29 Evidence Act 2023, section 135.
30 Abubakar Garba, 'Impediments to Effective Enforcement of Insider Trading Regulations in Nigeria' (2013) 3(1) *International Journal of Management* 19.
31 *United States v Gamache* 156 F. 3d 18 (1st Cir. 1988).
32 *SEC v Sargent* 229 F. 3d 68, 75 (1st Cir. 2000).
33 *Suberu v The State* (2009) LPELR-8716(CA).

framework has proven inadequate in effectively combating this pervasive practice. The lack of a standalone insider trading statute, coupled with weak enforcement mechanisms and inadequate penalties, has enabled insider traders to operate with impunity, jeopardizing the integrity of the capital market. Combating insider trading requires a concerted effort from regulators, companies, and investors.

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