THE INSIDER TRADING PROVISIONS OF THE FEDERAL CORPORATIONS AND SECURITIES INDUSTRY BILL, 1975[1]

Late in 1970, I wrote a paper on the control of insider trading for a series of lectures on the New South Wales *Companies (Amendment) Bill* 1970. That Bill, amongst other things, proposed:

(i) Amendments to the *Companies Act* 1961 (NSW), section 126 and 127, concerned with disclosure of directors' shareholdings;
(ii) The addition of a new Division 3A of Part IV to the Act so as to impose a duty on a company to maintain a register of substantial shareholdings and of substantial shareholder transactions, and so as to impose duties on substantial shareholders to disclose their holdings and transactions to the company;
(iii) Amendments to section 124 of the Act, concerned with the duty of a company officer not to make improper use of information acquired by virtue of his position, and his liability to the company for any profit made by him by such use; and
(iv) The addition of a new section 124A to the Act which would have imposed a liability on a company officer, who in dealing in the securities of his company made use of special confidential information, to compensate another person who suffered loss by paying too much for those securities.

The amendments proposed were intended to give effect to recommendations of the Eggleston Committee in is Second and Fourth Interim Reports. My paper endeavoured to assess the effectiveness of the proposed amendments in strengthening the controls on insider trading. The changes in fact made in the law—in 1971—in some respects differed materially from those proposed by the New South Wales *Companies (Amendment) Bill.* The amendments to sections 126 and 127 of the *Companies Act* were made and Division 3A relating to substantial shareholdings was adopted. However, the proposed section 124A was not enacted. Instead a new section 75A was inserted in the *Secruities Industry Act* 1970 (NSW). This section was made

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1 This article is substantially reproduced from a paper delivered by the author at a seminar held at the Sydney University Law School in August 1975.

the primary control on insider trading. Section 124 of the *Companies Act,* while amended as had been proposed, was given only a subordinate role. An officer is not guilty of an offence under Section 124 or liable to account to the company under that section, if his conduct is an offence under section 75A of the *Securities Industry Act.*

The present article is concerned with the sections of the Federal *Corporations and Securities Industry Bill* 1975 which relate to the control of insider trading. These are:

(i) S 50 which empowers the making of regulations which will impose duties on directors and other prescribed officers of a registered corporation to lodge with the proposed Federal Corporations and Exchange Commission such written reports as may be prescribed concerning their interests in the securities of the corporation;

(ii) Part IX of the Bill which requires notification to the company and to the Commission of substantial shareholdings and changes in shareholdings in registered corporations whose shares are permitted to be traded on a registered stock exchange;

(iii) Sections 123, 124 and 125, and some ancillary sections, which prohibit dealings by insiders in the securities of prescribed corporations. 'Prescribed corporations' is widely defined so as to embrace any corporation in relation to which the Commonwealth has constitutional power to legislate.

It will be helpful in considering the provisions of the 1975 Bill to make some observations on the present New South Wales law and to look briefly at recent developments in the United Kingdom, Ontario and the USA. Comparison with the New South Wales law and the laws of these other countries may serve to sharpen our understanding of the likely operation of the provisions of the 1975 Bill and to assist our evaluation of them.

I should say that, for purposes of this article, I accept the need for some provisions controlling insider trading, though I am conscious that this need is not as incontrovertible as is often assumed. A good deal of the condemnation of insider trading one hears is moved more by envy than by moral conviction. Far from condemning, there are others who would say that insider trading pushes market prices in the right direction and that profits from such trading are appropriate means of compensating the entrepreneur. And if one makes the case for control, as Louis Loss does, in terms of market egalitarianism, there remains the question of how much equality one should seek to achieve.

I

A SURVEY OF THE PRESENT NEW SOUTH WALES LAW

(1) *In relation to the disclosure of interests in company securites*

Section 126 of the *Companies Act* imposes an obligation on a company to keep a register showing in respect of each director of the company particulars of:

(a) Shares in the company or in a related company in which he has a relevant interest (in the very wide sense of those words in section 6A);

(b) Debentures or participatory interests (as defined in section 76) made available by the company or a related company in which the director has a relevant interest;

(c) Rights or options of the director in respect of the acquisition or disposal of shares, debentures or participatory interests in the company or a related company;

(d) Contracts to which the director is a party or under which he is entitled to a benefit, being contracts under which a person has a right to call for or to make delivery of shares, debentures or participatory interests in the company or a related company.

The company must record changes in interests and particulars of the transactions under which the changes occurred. The duty of a director to disclose his interests and changes in his interests is imposed by section 127.

The intention is to cover any interests whatsoever which a director might have in any kind of securities of his company or of a related company. Section 126, for example, will extend to interests under put or call option transactions into which the director has entered.

Sections 126 and 127 reflect the view of the United Kingdom Cohen Committee that 'the best safeguard against improper transactions by directors and against unfounded suspicions of such transactions is to ensure that disclosure is made of all their transactions in the shares or debentures of their companies'. But as a control on insider trading, the sections are limited in several respects. They relate only to directors, though other controls on insider trading, it will be seen, apply to a wider range of persons. The United Kingdom law in sections 27, 28 and 29 of the *Companies Act* 1967, while otherwise confined to directors, requires the interests of the wife or husband or of the infant child of a director to be treated as the interests of the director. Ontario law in sections 109 and 110 of the *Securities Act* requires disclosure

not only of directors' interests but also of interests of specified senior officers of the company and of persons holding 10% or more of voting rights in the company. The United States law in the *Securities Exchange Act* 1934, section 16(a), requires disclosure of interests of directors and officers and of shareholders holding 10% or more of the voting shares in the company, and the person who is obliged to disclose must include in his report information in relation to securities held by relatives who share his home.

The publicity given by section 126 to the interests disclosed by directors is limited. The register kept by the company must be open for inspection, and must be produced at the annual general meeting of the company. But this publicity is much less than is required by Ontario and United States law. Under the Ontario *Securities Act* section 111, the information supplied by the company officer must be filed at the Securities Commission and the Commission is required to maintain information for public inspection and to publish monthly summaries of new information. In the United States the information disclosed must be filed with the Securities and Exchange Commission and the Stock Exchanges, and is made available to the public at the office of the Securities and Exchange Commission and the Stock Exchanges. A monthly summary may be obtained from the Government Printing Office.

The substantial shareholder provisions adopted in 1971 were those proposed in the *Companies (Amendment) Bill* 1970 (NSW). So far as its purpose can be identified, the duty to disclose imposed on the substantial shareholder by Division 3A of Part IV of the *Companies Act* is not in its origin related to the control of insider trading, as is the duty to disclose imposed on directors. The substantial shareholder provisions have however come to be linked with control of insider trading by the definition of 'associated person' in section 75A of the *Securities Industry Act*. The substantial shareholder disclosure provisions in the Ontario and in the United States law have always been aspects of the control of insider trading.

A person is a substantial shareholder for purposes of Division 3A if the aggregate of the nominal amounts of the voting shares in which he has interests is not less than one-tenth of all the voting shares in the company or of the class of voting shares in which he has interests. He must give notice to the company of his shareholding and of changes in his shareholding within 14 days and the company must maintain a register. The register must be available at the company's

registered office on much the same terms as the company's share register.

The substantial shareholder provisions of the New South Wales *Companies Act* correspond, generally, with ss 33 and 34 of the United Kingdom *Companies Act* 1967.

(2) *In relation to dealing in securities*

Under section 75A of the New South Wales *Securities Industry Act* 1970 a person who is associated with a company is guilty of an offence in the following circumstances:

> He must have, through his association, knowledge of specific information relating to the company or to securities issued and made available by the company which is not generally known but, if generally known, might reasonably be expected to affect materially the market price of those securities.

And he must either

> (a) deal, directly or indirectly, in those securities for the purpose of gaining an advantage of himself by the use of that information; or
> (b) divulge that information for the purpose of enabling another person to gain advantage by using that information to deal, directly or indirectly, in those securities.

The penalty provided is a fine of $2,000.

Where an offence has been committed by the associated person having dealt for his own benefit in the securities, there may be an action against the associated person by the person who has suffered loss, or by the company. Where the offence is divulging, there may be an action against the person who dealt to his advantage by the person who in the result suffered loss, or by the company.

The section has a wide application in respect of the range of persons who may be guilty of an offence. The concept of an associated person is defined in sub-section (6). It includes:

> (i) An officer of the company or a related company;
> (ii) A person who acts or has acted, as banker, solicitor, auditor or professional adviser, or in any other capacity, for the company;
> (iii) A person who has a beneficial interest in shares whose nominal amount is not less than one-tenth of the aggregate of the nominal amounts of all the issued shares of the company; or
> (iv) A person who is a director manager or secretary of a company which is associated in virtue of (ii) or (iii) above.

It may be noted that a person who at the time of the dealing had ceased to be an officer is not included, though, curiously, a person who has ceased to act as banker, solicitor etc. is included.

The associated person must have knowledge of 'specific' information which is not 'generally known but, if generally known, might reasonably be expected to affect materially the market price of (the) securities'. He must have dealt for the purpose of gaining an advantage for himself, or have divulged for the purpose of enabling another person to gain an advantage. The word 'specific' has some limiting operation. The word has been taken from the Ontario *Securities Act,* section 113, which in this respect, has been the subject of judicial interpretation to which I will make later reference. Nonetheless, it probably has a less limiting operation than the word 'special confidential' which were used in the section 124A which it was proposed to include in the *Companies Act* by the *Companies (Amendment) Bill* 1970 (NSW). No attempt is made to define 'generally known'. 'Divulged' presumably means something more than the giving of a general tip, for example, that some security is a good buy, or one which should be sold now. One neither acts to gain advantage for oneself nor divulges if one acts as agent for another (for example, as agent for one's wife or as a company in which one is not interested), or as trustee for another (for example, as trustee of a family trust).

It is at least arguable that section 75A has no application to a dealing by entering into a put or call option transaction. The definition of security in section 4 is wide enough to include rights under a put or call option, but these rights are not 'issued or made available by the company'. It might be thought that the option transaction could be treated as a dealing in the shares to which it relates, but this would produce an absurd result in the application of other provisions of section 75A.

The associated person must have dealt for the purpose of gaining an advantage for himself by the use of the information or have divulged for the purpose of enabling another person to gain an advantage by using that information. Mere dealing while having knowledge of specific information, or divulging specific information, is not enough. No offence is committed by a person to whom information has been divulged by an associated person, even though he deals for the purpose of gaining an advantage.

An action lies against an associated person who has committed an offence by a dealing to his own advantage. The action may be brought by the person who incurred a loss as a result of the gaining of the advantage by the associated person, to recover the amount of that loss. Alternatively, an action may be brought by the company to recover

from the associated person any profit that accrued to him by reason of the gaining of the advantage.

Where the associated person has divulged information in circumstances which amount to an offence, there is an action available to the person who suffered loss to recover the amount of the loss against the person who gained the advantage. Alternatively, there is an action available to the company to recover the amount of any profit that accrued to the person who gained the advantage.

The action available to the person, who suffered loss in either of the situations just described, will not be of any significance where the transaction by which he suffered the loss was carried out on a Stock Exchange. It will, save in a rare case, be impossible for him to establish that the person with whom he dealt was the person who gained the advantage to which the section refers. In any event, the fact that he dealt with the person who gained the advantage will be simply fortuitous, and it may be thought inappropriate that he should have any action.

Where the transaction was not on a Stock Exchange, the action available to the person who suffered a loss may be significant and appropriate. But there is acute difficulty in correlating the action available to him with the action available to the company to recover any profit made by the person who gained the advantage. The section gives no guidance as to whether priority is determined by being first to sue, or by some other test.

The action to recover a loss and the action to recover a profit are presumably to recover a loss or a profit deemed to have been incurred of the amount calculated in accordance with sub-section (3). This amount is the difference between the price at which the dealing was effected, and the price that in the opinion of the court before which it is sought to recover the amount of the loss of profit, would have been the market price of the securities at the time of the dealing if the specific information used to gain that advantage had been generally known at that time. The forming of an opinion by the court is likely to be a speculative exercise.

Sub-section (4) provides that the Corporate Affairs Commission, if it considers it to be in the public interest so to do, may bring an action in the name of and for the benefit of the person who has suffered loss, or the company, for the recovery of the amount of the loss or the amount of the profit. Without sub-section (4), neither the action to recover a loss nor the action to recover a profit would be of much significance. A person who has suffered a loss by having dealt with

another may be deterred by the risk of defeat even though he will recover for his own benefit. The company is unlikely to bring an action against one of its senior officers, and it is a senior officer who is most likely to have made a profit from insider trading. It is true that an individual shareholder can assert the company's right of action in a derivative suit. But he is unlikely to do so when he runs the risk of defeat and the payment of costs, and when, moreover, if he succeeds he recovers not for himself but for the company. How much significance the actions available to the person who has suffered loss and to the company to recover a profit may have, rather depends on how ready the Commission may be to take proceedings. Where the transaction was not on a Stock Exchange, the Commission is faced with the need to choose between proceedings on behalf of the person who suffered the loss and the proceedings on behalf of the company.

Section 75A refers to knowledge of specific information relating to the company, or to securities issued and made available by the company, with which a person is associated. Where the information which a person associated with the company has, relates not to that company but to another company whose shares are the subject of the dealing, section 75A will not have any application. The information may, for example, be that the company with which the person is associated is about to make a bid for the shares of the other company whose shares are the subject of the dealing.

There are time limits on the actions which may be brought under section 75A. These are two years from the date of the dealing or six months next succeeding the discovery of the relevant facts by the person who seeks to recover his loss, or by the company which seeks to recover the profit, which ever time first expires.

Where a dealing does not involve an offence under section 75A it may give rise to criminal or civil proceedings under section 124(2). Section 124(2), applies only where there is improper use of information by a person who is at the time an officer. It is not enough that he was formerly an officer. It applies only where the information improperly used has been acquired by virtue of the officer's position as an officer. The meaning of 'improper' calls for judicial explanation. It is assumed in this article that it is improper for an officer to use information acquired by virtue of his position when that information is not generally available. But the possibility cannot be dismissed that 'improper' would be construed in a way which would deny section 124 any role in controlling insider trading. It is enough that information has been used. The information need not be 'specific'. Breach of

section 124(2) involves criminal liability. The penalty is $2,000. And it involves the prospect of a civil liability, but only to the company. There is no action available to a person who may have suffered loss as a result of the officer's action.

Though confined to officers and giving a civil remedy only to the company, section 124 may sometimes supplement section 75A. Thus the section may apply where an officer has entered into a put or call option transaction. It may apply though the transaction is one in which the officer has acted to gain an advantage not for himself but for another person—where he acts as agent or trustee. It may apply where the officer has given a general tip—a recommendation to buy or sell—which does not amount to a divulging of information, that is if giving such a tip can be regarded as constituting a making use to gain an advantage for the person to whom the general tip has been given.

The civil remedy given by section 124 is to recover a profit—presumably in this context a realized profit arising from having bought and sold securities—and it is available only to the company. It will be a rare proceeding for reasons explained in relation to section 75A, and there is no provision in section 124 for proceedings to be brought by the Commission on behalf of the company.

The requirement of section 75A that the information be 'specific' and that the dealing or divulging should have been for the purpose of gaining an advantage, and the failure of section 124(2) to give a remedy to a person who has suffered loss are clearly intended. Other limitations on the control of insider trading by those sections cannot have been intended: for example, the failure of section 75A to extend to dealings by an associated person as agent or trustee for another, or to dealings by way of put or call option transactions, and the failure of section 75A and section 124(2) to cover dealings by a former officer. Comment on these limitations, whether intended or not, is best reserved until the detailed consideration of the provisions of the *Corporations and Securities Industry Bill.*

II

SOME RECENT DEVELOPMENTS IN THE UNITED KINGDOM, ONTARIO AND THE U.S.A.

The United Kingdom

In a White Paper published in 1973 (Cmnd. 5391, July, 1973) the then Conservative United Kingdom Government set out views on company law reform, including the matter of insider trading. The White Paper expressed the Government's conclusion that the system

of control by the rules of the Stock Exchange, and by the Takeover Panel in bid situations should be reinforced by statute 'so as to ensure, as far as practicably possible, that the market operates freely on the basis of equality between buyer and seller' (Para. 15).

The White Paper made a number of observations on the United Kingdom provisions in regard to disclosure of directors' shareholdings and transactions in shares, provisions which are substantially the same as the New South Wales provisions in sections 126 and 127 of the *Companies Act*, to which reference has been made in Part I. The White Paper observed that the period of 14 days within which notification to the company is required is too long a period and the Government proposed to require notification within the shortest practicable period. It also referred to an offer of help by the Stock Exchange which had undertaken to publish details of transactions by shareholders in their company's securities if the law were amended to require notice to be given not only to the company but also to the Stock Exchange.

The White Paper proposed the reduction of the theshold percentage at which a holding and changes in holding have to be notified to the company and by requiring that notification be much quicker. The test of substantial shareholding proposed was 5% and the time to be allowed for notification, it was thought, should be 'the minimum consistent with practicable operation'.

'The object of legislation on insider dealing', the White Paper said 'must be to ensure that anyone who is in possession of information which would be likely, if generally known, to have a material effect on the price of the relevant securities refrains from dealing until the material information has properly been made generally available' (Para. 17). The White Paper proposed a definition of an insider so that it would 'include directors, employees, major shareholders and professional advisers of a company, together with the near relations of each of these people'. It further proposed, apparently unconscious that a wider notion of insider was thus being adopted, that 'dealing in a company's securities by anyone who, by reason of his relationship with a company or with its officers, has information which he knows to be price-sensitive should be a criminal offence unless he can show that his primary intention in dealing at that particular time was not to make a profit or avoid a loss' (Para. 18).

The White Paper proposed that 'the law should . . . confer a civil remedy on persons who can establish that by reason of the misuse of materially significant information they have suffered an identifiable

loss. Similarly, the law should preserve the present position whereby an insider may be accountable to the company for his profit' (Para. 19). There is no consideration in the White Paper of the problem of correlating the remedy available to a person who has suffered loss and the remedy which may be available to the company.

The White Paper was followed by publication of the *Companies Bill* 1973. Because of the change in government which thereafter occurred, that Bill was not proceeded with. The insider trading provisions of the Bill are, however, the source of much of the drafting of corresponding provisions in the Federal *Corporations and Securities Industry Bill* 1975. Some account of the provisions of the United Kingdom 1973 Bill will emerge from the study of the Federal Bill and the comparisons that will be drawn with the United Kingdam Bill in Part III of this article. One point might however be made at this stage. It is doubtful whether the drafting of the 1973 UK Bill, section 14(1), imposes an onus on the accused in criminal proceedings to show that his primary intention was not to make a profit or avoid a loss, though the White Paper proposed that he should carry such an onus. The Confederation of British Industry in the Report of its Company Affairs Committee in September 1973 had criticised the proposal in the White Paper.

The United Kingdom Labour Government published in May 1974 a Green Paper on the Reform of Company Law. The paper is the Report of a Working Group of the Labour Party Industrial Policy Sub-Committee. The observations in the Green Paper on the 'Tory Bill' of 1973 in its insider trading provisions, are generally approving. There is however a criticism (at page 35) of the exemption given by the Bill to the trustees of company pension schemes, and there is a call for a change in the Stock Exchange practice so that it will be possible to identify the parties to a Stock Exchange transaction (at page 36). The assumption in the call for a change in Stock Exchange practice is that it is appropriate to give the person who has dealt with an insider in a Stock Exchange transaction a civil remedy available against the insider.

Ontario

The Ontario law[2] imposes duties of disclosure and gives civil remedies to persons with whom an insider has dealt, and also to the company.

2 *Securities Act* 1966 (Ontario). The relevant provisions of this Act are set out in an Appendix to this article.

The insider trading provisions of the Ontario law have been the subject of criticism, and proposals for change are made in the 1973 Report on Mergers, Amalgamations and Certain Related Matters, by a Select Committee on Company Law of the Legislative Assembly. The Report draws attention to the fact that under the Ontario law 'professional advisers or consultants retained by a corporation, employees who are neither directors nor senior officers, and the vaguely defined group of persons sometimes know as "tippees" are all excluded from liability, unless they happen to be an associate of an insider' (at page 62). The Committee expressed the opinion that these persons should be subject to the same liability as a director or senior officer. The Report also drew attention to the possibility that directors and senior officers of an offeror corporation about to make a takeover bid may trade in the shares of the offeree corporation prior to the bid being made, based on their knowledge of the terms of the bid. The Committee expressed the view that the provisions of the legislation on insider trading should be enlarged to cover this situation (at page 63).

It will be noted that the Ontario law provides that on the application of any person who was the owner of securities of a corporation at the time of the transaction complained of, the Court may make an order requiring the Ontario Securities Commission to commence or to continue an action, in the name of and on behalf of the corporation, to enforce the liability of the insider. The Report expressed the view that the Securities Commission should have the right to apply to the Court to obtain the required order (at page 64).

A number of comparisons with the Ontario law are drawn in the account, in Part III of this article, of the provisions of the Federal Bill.

The United States

The development of the United States insider trading law continues in a number of decisions arising out of the circumstances of the *Texas Gulf Sulphur Case*.[3] Most important is a decision by Bonsal J on remand from the Circuit Court of Appeals, by which the insiders were ordered to pay Texas Gulf Sulphur the difference between the price at which they purchased Texas Gulf Sulphur stock and the mean price on the day after the announcement by which news of the nickel strike was made public, with 6% interest on that amount for the period between purchase day and the day of the announcement. Amounts

[3] (1968) 401 F 2d 833. Affirmed (1971) 446 F 2d 1301.

recovered by the company were directed to be held in escrow for five years, presumably in order that anyone who had purchased from an insider might prove this to the company and be compensated from the amounts recovered.

In addition there have been decisions as to when transactions by tippees may be unlawful under Rule 10(b)(5) and on other aspects of the interpretation of the Rule.[4] There have also been news decisions on general equity principles which bear on insider trading.[5] It should be noted that the availability of general equity principles has not been affected by the statutory provisions which have been adopted in the United States, or for that matter in the United Kingdam, in Ontario or in the Australian states. A decision by the courts to overrule *Percival v Wright*[6] would simply add a course of action to those open under the statutory provisions to the person who has dealt with an insider, and make more necessary some correlation between the actions available to the person who has dealt and any actions under the general law or statute available to the company.

The most important development in the United States law-making has been the preparation of drafts of the American Law Institute's proposed Federal Securities Code. The American Law Institute and its *Draft Securities Code* are described in Professor Loss's Memorandum to the Australian Government on Proposals for Australian Companies and Securities Legislation (at pages 1-2). Professor Loss is the reporter to the Law Institute's undertaking. A Reporter's Revision of the texts of tentative drafts Nos. 1-3 was released on October 1, 1974. Included in the revision are Parts XIII and XIV which cover the restatement of the law developed from Rule 10 (b) (5) and the civil remedies for breach of the Rule. In the course of Part III of this article, in commenting on the Federal Bill, I have made comparisons with the law as proposed in Parts XIII and XIV, both because it may be assumed that the *Draft Securities Code* is likely to become the US law, so far as it may not already be so, and because the Code offers a coherent statement of principles in statutory form with which a comparison of principles in the Federal Bill may the more usefully be made.

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4 Shapiro v Merrill Lynch (1973) F Supp 264; Affiliated Ute Citizens v U S (1972) 406 U S 128.

5 Eg Schein v Chasen (1973) 487 R 2d 817.

6 (1902) 2 Ch 421.

III

THE PROVISIONS OF THE CORPORATIONS AND SECURITIES INDUSTRY BILL 1975

(1) *In relation to the disclosure of interests in company securities*

Section 50 of the Bill provides that a director of a registered corporation, and each other officer of the corporation included in a prescribed class of officers of the corporation, shall, whenever required to do so by or in accordance with the regulations, lodge with the Commission (The Corporations and Exchange Commission) such written reports as are prescribed concerning his interests in securities of the corporation and of any related corporation of which he is a director or other officer. The provisions of section 17, defining when a person has an interest in a share, are to have effect so far as the section is capable of application for the purposes of section 50, as if references in section 17 to a share or shares were references to a security or securities (s. 50(2)).

The section empowers the making of rules and regulations which could require wider disclosure and a greater publicity for the information disclosed than under the NSW *Companies Act* sections 126 to 127. The latter sections require notice to the company of transactions by directors in company securities within 14 days of the transaction and the keeping of a public register by the company of such transaction. The 1973 UK White Paper proposed notification under the equivalent provisions of the UK law should be made within 'the shortest practicable period' and referred to an undertaking by the Stock Exchange to publish details of such transactions if the law were amended to require notice to be given simultaneously to the Stock Exchange. The United Kingdom 1973 Bill, Section 17, proposed notification within three days and that the director be required to notify the Stock Exchange as well as the company. The Stock Exchange would be empowered to publish this information.

Section 50 of the Federal Bill contemplates notification not only by directors but also by 'a prescribed class of officers'. The Bill has apparently in mind the Ontario and United States' models.

Section 50 will not require the disclosure of interests of members of the family of the company officer, and in this respect it is more limited in its requirements than is the United Kingdom law. The provisions for notification will not therefore assist in detecting transactions in which an officer acts as agent for a member of his family or, save in circumstances where he is taken to have an interest by

virtue of the definition of Section 17, where he acts as agent for a family company or as trustee.

The definition of interests in section 17 is not in its terms wide enough to include rights under a put option. But it would not follow that the rules may not prescribe that a report be given of a transaction involving a put option. Section 50 provides for reports as are prescribed concerning the officers' interests in securities. The giving of a put option would concern his interest in the shares the subject of the option. The NSW Act, section 126(1) (d), expressly requires notification of put option transactions.

The provisions in Part IX of the Federal Bill relating to the disclosure of substantial shareholdings and changes in holdings are based on existing provisions of State legislation and substantially follow the provisions of Division 3A of Part IV of the NSW *Companies Act*. Part IX of the Bill does however adopt the proposals of the UK White Paper and the 1973 UK Bill by reducing the threshold, at which notification becomes necessary, to 5% of nominal capital of voting shares, and by reducing the time within which notification must be made to 3 days. Notification is to be given to the company and to the Corporations and Exchange Commission. The latter notification is a new development. Notifications to the Commission will be available for public inspection.

(2) *In relation to dealings in securities*

The explanatory memorandum which accompanies the Federal Bill asserts that the 'strong provisions with respect to insider trading' which have been included 'are largely based upon the insider trading provisions included in (the) United Kingdom Companies Bill introduced in 1973'. While much of the drafting of the Federal Bill is clearly taken from the United Kingdom Bill there are some fundamental differences in effect which might justify questioning the assertion in the explanatory memorandum. In what follows the provisions which prohibit conduct held to amount to insider trading are first considered and thereafter the consequences of contravention of these provisions. The principal comparisons drawn in commenting on the Bill are with the United Kingdom Bill. At the same time comparisons are drawn with the NSW and Ontario law, and with the United States *Draft Securities Code*.

(a) SECTION 123(1)

A person who is, or at any time in the preceding 6 months has been connected with a prescribed corporation shall not deal in

> *any securities of that corporation if by reason of his so being, or having been, connected with that corporation he is in possession of information that is not generally available but, if it were, would be likely materially to affect the price of those securities.*

Section 123(1) follows generally the provisions of section 12(1) of the United Kingdom 1973 Bill.

The meaning of 'deals in securities' is given in section 106(1) as follows: 'A person deals in securities if and only if (whether as principal or as agent) he buys, sells or subscribes for, or agrees to buy, sell or subscribe for, any securities'. 'Securities' is defined in section 3 to include 'units' and 'units' is defined in the same section, in relation to a share or debenture, to mean 'any right or interest in the share or debeture, by whatever term called'. Section 17, to which reference has already been made, is attracted by section 106(3) and may extend the meaning of 'interest' in the definition of 'unit'. Nonetheless there is room to argue that the prohibition in section 123(1) does not extend to the taking of an option from the company to subscribe for shares in pursuance, for example, of an employee share option scheme. One aspect of the insider trading of the senior employees in *Texas Gulf Sulphur*[7] was the taking of share options offered by the company at a time when knowledge of the nickel strike had not yet been communicated to the members of the board of directors of the company. The argument would be that one does not buy a right if the concluding of the transaction brings that right into existence. The like argument might be made in relation to the issue by the company of rights to shares. And it might also be argued, perhaps with greater force, that the taking of a put or a call option offered by a share option dealer is not covered by section 123(1). The sale of right or option after it had been issued by the company, would be covered. The sale of a call option already issued by a dealer would presumably be covered: it might be noted that there is a move to extend trading facilities of the Austrailan Stock Exchanges to include trading in such options. But the sale of a put option may not be covered. A put option, it is suggested, is not a security. It would be argued that a right to sell shares is not a right or interest in shares. The definition of 'interest' in section 17 does not appear wide enough to include such a right.

The provisions of the United Kingdom 1973 Bill may similarly be limited in their operation. And it has been submitted that there are limits of this kind on the operation of the NSW legislation, more

[7] (1968) 401 F 2d 833. Affirmed (1971) 446 F 2d 1301.

particularly section 75A of the *Securities Industry Act.* The Ontario *Securities Act* would appear to achieve an operation not subject to such limitations by an interpretation provision (section 109(2)(b) that the 'acquisition or disposition . . . of a put, call or other transferable option with respect to a capital security shall be deemed a change in the beneficial ownership of the capital security to which such transferable option relates'. It will be recalled that the operative provision of the Ontario Act (section 113) provides, so far as presently relevant, that 'every insider . . . , who, in connection with a transaction relating to the capital securities of the corporation makes use of any specific confidential information . . . ' commits a breach of duty. The relevant operative provision of the US *Draft Securities Code* makes it 'unlawful for an insider to sell or buy a security of the issuer' in defined circumstances (section 1303(a)). The definitions in sections 293 and 283 of 'sell' and 'buy' and the definition of 'security' in section 297 are, it is thought, wide enough to overcome the limitations to which section 123(1) of the Federal Bill may be subject. Section 293(f) provides that 'sell' includes 'the issuance of a security', and section 283 provides that 'buy' has a correlative meaning.

The word 'information' in section 123(1) of the Federal Bill is not qualified by any adjective. It would presumably have a wider meaning therefore than the words 'specific information' which are used in section 75A of the NSW *Securities Industry Act,* and an even wider meaning than the words 'specific confidential information' which appear in the Ontario *Securities Act.* There is an Ontario decision[8] that knowledge that negotiations as yet inconclusive are going on, with a view to a takeover bid, is not 'specific information'. The absence of the word 'confidential' will preclude any argument that section 123(1) cannot apply in regard to information which could be disclosed without breach of confidence. The United States *Draft Securities Code,* section 1303(a) uses the language 'if he knows a fact'. 'Know' and 'fact' are defined very widely. Thus section 251A provides that 'know' . . . includes 'awareness by a person of a high probability of the existence or non-existence of a particular fact, unless he actually believes the contrary'. By section 234A 'fact includes a promise, prediction, estimate, projection, or forecast, or a statement of intention, motive, opinion or law'.

Presumably, 'in possession of information' would be given as wide a meaning as the definitions of 'know' and 'fact' give the United

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8 Green v Charterhouse Group Canada Ltd et al (1973) 35 DLR 3d 161.

States language 'knows a fact'. There is no case for limiting the 'information' which is relevant to that which is intrinsic to the corportion, for example a nickel strike, and excluding extrinsic information, for example that a leading firm of investment analysts are about to issue a report recommending purchase of the securities.

Limits by reference to 'specific', 'special' and 'confidential' may be thought to confine the operation of insider trading provisions in an inappropriate way. The more appropriate limits are those which go to whether the information is already public and to its likely influence on the price of the securities. Section 123(1) requires that the information be information 'not generally available' which, 'if it were (available), would be likely materially to affect the price of (the) securities' to which the prohibition relates. The phrases used in section 75A of the NSW *Securities Industry Act* are 'not generally known', which may be more restrictive than the corresponding phrase in section 123(1), and 'might reasonably be expected to affect materially the market price of (the) securities'. The drafting of that section was taken from the Ontario *Securities Act*. Section 106 of the Federal Bill defines 'generally available' where the securities are not permitted to be traded on a stock exchange; otherwise, neither of the phrases presently under discussion is defined. The phrase 'not generally available' may be thought to be rather more indeterminate than is appropriate. Unless it is the intention to provide that the connected person with information must deal at his peril, some test of 'generally available' should be included. In *Texas Gulf Sulphur*[9] there were a number of dealings during and immediately after the announcement of the nickel strike, and members of the Circuit Court of Appeals speculated about how much time must elapse after a public announcement before information may be said to be 'effectively disclosed'.

Section 1303(a) of the US *Draft Securities Code* makes it unlawful for an insider to sell or buy a security of the issuer, if he knows a fact of special significance with respect to the issuer or the security 'that is not generally available'. The Code brings a measure of determinacy by defining the phrase 'generally available' in Section 1303(d) as follows: 'A fact is generally available when (1) it is disclosed in a filing or is otherwise disclosed by means of a press release or other form of publicity reasonably designed to bring the fact to the attention of the investing public, and (2) one week or any other period that the Commission' (that is the Securities and Exchange Commission) 'pre-

[9] (1968) 401 F 2d 833. Affirmed (1971) 446 F 2d 1301.

scribes by rule has expired since the filing or other disclosure'. The definition goes on to provide that 'when these conditions are not satisfied, the burden of proving that a fact is generally available is on the person who so asserts'.

Where the securities are not permitted to be dealt in on a stock exchange section 106(2) of the Federal Bill provides that 'not generally available' refers to 'not being available to all the parties to the transaction in question'. The meaning thus given to 'generally available' nonetheless leaves considerable uncertainty.

The application of the notion of information 'likely materially to affect the price of (the) securities' will require resort to the speculation which makes up the art of the market analyst. The 'price' referred to where the securities are traded on a stock exchange is presumably the price on that exchange. This is the inference from Section 106(2) which provides that where the securities are not so traded the 'price' refers to 'the price at which the securities are dealt in under (the) transaction'. This would appear to require a judgment that what would have been paid in the actual transaction would have been different if all the parties had had the information.

Where the shares are traded, it is a matter not of what would happen in a wholly national market, if such could be imagined, but of what is likely to happen. It may be that knowledge of as yet inconclusive negotiataions about a take-over bid, or the result of a single drill core in mining exploration, are not such as would, in a rational world, affect the price of securities. But it seems, from experience, that general knowledge of matters of these kinds does in fact affect the price of securities.

The equivalent in the United States *Draft Securities Code* Section 1303(a) of the words 'information . . . likely materially to affect the price of securities' is 'a fact of special significance'. This phrase is defined, though one might doubt whether the definition brings any great measure of certainty to the operation of the section. It is provided in section 1303(c) that a fact is of special significance 'if (1) in addition to being material it would be likely on being made generally available to affect the market price of a security to a significant extent, or (2) a reasonable person would attach special importance to it in determining his course of action in the light of such factors as the degree of its specificity, the extent of its difference from information generally available previously, and its nature and reliability'. 'Material' is itself defined in section 256 thus: 'a fact is material if a reasonable person would attach importance to it under the circum-

stances in determining his course of action'. The language of the U.S. *Securities Code* may be more restrictive than that used in the Federal Bill. 'Significant extent' and 'special importance' suggest that a likely substantial affect on the price of the securities must be shown.

Section 123(1) prohibits a dealing while a connected person is in possession of information which is not generally available, whatever the purpose of that dealing. This involves a most significant difference between the law as proposed in the Bill and the law in the provisions of the NSW Acts. Under Section 75A of the NSW *Securities Industry Act* the insider must have dealt 'for the purpose of gaining an advantage for himself' or have divulged 'for the purpose of enabling another person to gain an advantage'. Under Section 124(2) of the NSW *Companies Act* the officer must have made improper use of information 'to gain an advantage'. Requiring that a purpose to gain an advantage must be shown, is a limitation on the application of these sections even though the law may place the burden of explanation on the insider. The Ontario Court assumed that the law placed the burden of explanation on the insiders in the *Charterhouse Case.*[10] It will be recalled that the Ontario law requires that the insider must have made use of the information for his own benefit or advantage. In *Charterhouse* the shares were traded on the stock exchange, but the particular dealings were off-market transactions between the plaintiff and other shareholders who were the defendants, and all of whom were parties to a buy-sell arrangement. The defendants were able to offer the explanation that the plaintiff's giving of a notice of intention to sell had forced them into a position where they had to purchase to avoid the plaintiff's shares being thrown on the market with resulting disturbance to the value of the company's shares on that market, and some detriment to the company. They were also able to say that they had acted to assist the plaintiff to get rid of his shares. The irrelevance of the insider's purpose and the irrelevance of his belief that the information was not material combine to make s 123(1) a powerful inhibition of any dealing by an insider. We are brought very near to law which would say that a person connected with a company should never deal in the company's securities. The economic consequences and policy of such a law are both obscure.

The United Kingdom 1973 Bill (section 14(1)) provides that nothing in the operative provisions relating to insider trading 'shall preclude a person from entering into any transaction if his purpose is

10 (1973) 35 DLR 3d 161.

not, or is not primarily, the making of a profit or the avoiding of a loss (whether for himself or another) by the use of any such information as mentioned in the (operative provisions)'. There is no corresponding provision in the Federal Bill. This is one of the differences which throw doubt on the statement in the explanatory memorandum that the provisions of the Bill are laregly based on the insider trading provisions of the United Kingdom Bill.

The strict liability imposed by the Federal Bill has, however, support in the provisions of the US *Draft Securities Code*. Under that Code it is unlawful to deal with knowledge whatever the purpose of the dealing. It may be said, in defence of the drafting of the Federal Bill, that an insider in possession of information who does not seek to gain an advantage by dealing should see to it that the other party to the transaction is in possession of the information. This injunction is hardly appropriate when disclosure of the information would be a breach of confidence, though as a general proposition it may be fair enough to say that where disclosure would be a breach of confidence the insider must simply refrain from dealing, whatever his purpose in dealing might have been. And when it is recalled that it is irrelevant whether or not the insider believes the information to be material, the irrelevance under section 123 of his purpose makes the provisions of the section a powerful inhibition to any dealing by an insider. We are brought very near to an expression of a policy that a connected person should never deal in the company's securities—a policy whose economic consequences are unknown and whose morality is obscure.

The prohibition of section 123(1) is directed to a person 'who is, or at any time in the preceeding 6 months has been, connected with a prescribed corporation'. The notion of 'connection with (the) corporation' is defined in sub-section (7). A corporation cannot be a 'connected person'. The controls on insider trading by a corporation, it will be seen, are provided in sub-section (3) and sub-section (6) of section 123. In not applying the basic control on insider trading provided by section 123(1) to a corporation, the Federal Bill differs significantly from section 75A of the NSW *Securities Act*. Under the latter Act a corporation can be an 'associated person'—the notion under that Act equivalent to a 'connected person'. Both the Ontario *Securities Act* and the United States *Draft Securities Code* apply the basic control to a company which is an insider.

By subsection (7) of section 123 of the Federal Bill an individual may be connected with a corporation where—

'(a) he is an officer of that corporation or of a related corporation;

(b) he is a substantial shareholder within the meaning of Part IX in that corporation or in a related corporation; or
(c) he occupies a position that may reasonably be expected to give him access to information of a kind to which sub-sections (1) and (2) apply by virtue of—
  (i) any professional or business relationship existing between himself (or his employer or a corporation of which he is an officer) and that corporation or a related corporation; or
  (ii) his being an officer of a substantial shareholder within the meaning of Part IX in that corporation or in a related corporation.'

The notion of a connected person is thus very widely drawn. It will cover the consulting geologist, the underwriter, the investigating accountant and the auditor. And the phrase 'business relationship' opens up the prospect that any individual who makes a contract of more than a routine nature with a corporation may become subject to the prohibition of Section 123(1) in relation to dealings in the securities of that corporation.

The Ontario notion of insider to whom the general prohibition of the law is applied is more limited in its application than the notion of insider for purposes of section 123(1) of the Federal Bill. A professional or business relationship of a person with a corporation in whose securities the person has dealt, will not make him an insider. The United States *Draft Securities Code,* on the other hand, would apply its section 1303 (a) to any person whose relationship to the corporation gives him access to a fact of special significance. This drafting is not, it seems, intended to be as wide as the drafting of the Federal Bill in its reference to a 'position' giving 'access to information . . . by virtue of any professional or business relationship' but it is difficult to see why it is not in fact as wide. Comment 5 (e) to section 1303 of the US Draft Code observes that 'it would be convenient to have a new category of "quasi-insider" that would cover people like judges' clerks who trade on information in unpublished opinions, Federal Reserve Bank employees who trade with knowledge of an imminent change in the margin rate . . . and perhaps persons who are about to give profitable supply contracts to corporations with which they are not otherwise connected'. The illustrations of the judge's clerk and the Reserve Bank employee will be governed by section 124 of the Federal Bill, considered later in this article. The illustration of the person who is about to give a profitable supply contract would, it is thought, be covered by section 123(1).

Paragraph (c) of subsection (7) of section 123 of the Federal Bill gives a wider meaning to 'connected person' than section 75A(6) gives to the comparable notion of 'associated person' in section 75A of the NSW *Securities Industry Act.* Sub-section (7) (c) of section 123 of the Bill requires only a professional or business relationship. Sub-section (6) of section 75A refers to acting in various capacities *for* the corporation. Sub-section (7)(c) of the Federal Bill would extend to an employee of a person with a professional or business relationship to the corporation. Sub-section (6) of section 75A extends to a director, manager or secretary of a corporation acting for another corporation in one of the various capacities; but it will not extend to any other employee of a person acting for the other corporation. The extension of 'connected person' by sub-section (7)(c) to include an employee of a person with a professional or business relationship to the corporation in whose shares the employee has dealt, probably goes further than the law proposed in the US *Draft Securities Code,* unless the notion of relationship in section 1303 (a) in that Code is to be regarded as wide enough to pick up the vicarious relationship which the employee of one person may be thought to have with the person with whom his employer has a relationship.

The time limit of six months within which a person who was formerly a connected person would remain subject to the prohibition of section 123(1) of the Federal Bill is a significant limitation on the operation of the section. The New South Wales legislation draws, it will be recalled, a somewhat curious distinction so that an officer will cease to be subject to the operation of either section 75A of the *Securities Industry Act* or of section 124 of the *Companies Act* when he ceases to be an officer, but other persons may continue to be treated as associated without time limit. One would have thought that ceasing to be connected should not of itself relieve of liability where the person is in possession of information because he was connected with a corporation. At some stage the information will become generally available, but until then the prohibition should subsist. This is the approach of the US *Draft Securities Code.* It is hardly appropriate than an officer of a company should become free to deal six months after ceasing to be an officer in circumstances such as *Texas Gulf Sulphur*[11] where the period between the time when the information first becomes known to an officer and the time when it becomes generally available may well exceed six months.

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11 (1968) 401 F 2d 833. Affirmed (1971) 446 F 2d 1301.

The prohibition in section 123(1) extends only to information of which the connected person is in possession by reason of his being so connected or having been so connected. A similar limitation applies in relation to the NSW sections. The Ontario *Securities Act* does not have any explicit provision to this effect, but it may follow from the restriction of the prohibition to 'confidential' information. The *United States Code* draws a distinction. Where the dealing is by a person who is at the time a director or officer, it will be unlawful even though his knowledge of the fact of special significance does not arise by virtue of his occupying that status. Where, however, the dealing is by a person whose relationship or former relationship (which would presumably include a former status as director or officer) to the corporation gives or gave him access to a fact of special significance it will be unlawful only if he knows the fact of special significance by virtue of that relationship.

(b) SECTION 123(2)

A person who is, or at any time in the preceding 6 months has been, connected with a prescribed corporation shall not deal in any securities of any other prescribed corporation if by reason of his so being, or having been, connected with the first-mentioned corporation he is in possession of information that—

(a) is not generally available but, if it were, would be likely materially to affect the price of those securities; and

(b) relates to any transaction (actual or expected) involving both those corporations or involving one of them and securities of the other.

Section 123(2) follows generally section 12(2) of the United Kingdom 1973 Bill.

The obvious illustration of circumstances to which section 123(2) is applicable is a dealing by an officer of a bidding corporation in the shares of the target corporation. It will apply where an officer of a corporation deals in securities of another corporation and his corporation either expects to enter or has entered into a contract with that other corporation. The contract would of course need to be of such significance that knowledge of it would be likely materially to affect the price of the securities in the other corporation.

There is some overlap between section 123(2) and section 123(1). The definition of 'connected person' in sub-section (7) will extend sub-section (1) to a situation also covered by sub-section (2), i.e. where a person is an officer of a corporation which has a business relationship with another corporation in whose securities he deals. But sub-section (2) will have a significant operation exclusively its

own. In addition to the obvious situation of the take-over bid, it will, for example, cover the situation of a professional adviser to one corporation who as a result of his connection with that corporation, comes to be in possession of information relating to a transaction with another corporation in whose securities he deals. But it may not thus embrace the accountant advising a corporation on a proposal that it should underwrite an issue of shares in another corporation who comes to have information about the finances of the issuer. Information about the finances of the issuer does not relate to the underwriting transaction. Yet one would have thought that a prohibition direced to the accountant against dealing in shares of the issuer is more appropriate than the prohibition directed to the officer of the bidder against dealing in shares of the target corporation.

Section 75A of the New South Wales *Securities Industry Act* covers some of the ground that would be covered by Section 123(2) of the Federal Bill. By virtue of sub-section 6(e) of section 75A, that section will extend to a person who is director, manager or secretary of a corporation which 'acts or has acted as banker, solicitor, auditor or professional adviser, or in any other capacity' for another corporation in whose securities the person has dealt. But it will not cover the case of the investigating accountant advising a corporation on a proposal to underwrite an issue of shares in another corporation.

The Ontario *Securities Act* has no provision comparable with section 123(2) of the Federal Bill. The US *Draft Securities Code,* section 1303, would not appear to go as far as covering the investigating accountant in the underwriting illustration unless the circumstances were regarded as bringing about a relationship between the accountant and the company whose share issue is to be underwritten.

The extension of the scope of the notion of insider by section 123(2), and indeed some aspects of the notion as it is reflected in sub-section (1), raise the question of the policies sought to be served by insider trading provisions. One might be prepared to grant that there is a principle of commercial morality which precludes an officer or professional adviser of a company from exploiting knowledge about the company which he comes to have as an officer or adviser, where he exploits it to the advantage of himself or someone other than the company. But the policy of law which makes a person an insider simply because his employer has entered into a contract with another company in whose securities the person deals, or because his employer proposes to make a take-over bid for the shares in that company, is not very

evident, unless the policy is that anyone who has information which other persons do not have should be precluded from taking advantage of it. A principle that would assert that no-one who deals should have a better opportunity to gain than anyone else is either a *reductio ad absurdum* of an idea of equality or an expression of envy by the person of lesser opportunity who asserts it.

(c) SECTION 123(3)

Where a person is in possession of any such information as is mentioned in sub-section (1) or (2) (of section 123) in respect of any securities of a prescribed corporation but is not precluded by either of those sub-sections from dealing in those securities, he shall not deal in those securities if—

(a) he has obtained the information, directly or indirectly, from another person and knows that that other person is then himself precluded by sub-section (1) or (2) from dealing in those securities; and

(b) when the information was so obtained, he was associated with that other person or had with him an arrangement for the communication of information of a kind to which those sub-sections apply with a view to dealings in securities by himself and that other person or either of them.

Section 123(3) follows generally section 12(5) of the UK 1973 Bill.

The subsection is intended to impose a prohibition in relation to dealings by tippees. It extends to an indirect tippee—the tippee from a tippee—but only if he knows that the information comes from a tainted source, that is a person prohibited from dealing by sub-section (1) or sub-section (2).

The tippee must be in possession of information which he has obtained from another person. It would not appear that he can be in possession of information in the relevant sense if all that the other person has done is to recommend to him that he deal. Nor can he be in possession of information if he has guessed from the reactions of others that a dealing is likely to be advantageous. The solicitor who attended to the conveyancing involved in the acquisition of mining titles in *Texas Gulf Sulphur* had a 'readily inferable understanding' that shares in the company were a good buy, but it may be that he did not have information. The problems thus raised are parallel with problems of the meaning to be given to 'information' in sub-section (1). The fact that the word is not prefixed by the word 'specific' or 'special' is important in the present context, just as it is in relation to section 123(1).

The tippee must have 'obtained' the information and it is arguable that information which he has as the result of a shrewd guess has not been obtained.

A tippee may be prohibited by sub-section (3) from dealing in securities though the person from whom he obtained the information is not in breach of the prohibition against the communicating of the information imposed by sub-section (5) considered below. In this respect the prohibition on dealing imposed on the tippee is wider than that imposed by section 75A of the New South Wales *Securities Industry Act,* which imposes a prohibition on dealing by a tippee only when the person who 'divulged' information to the tippee did so in circumstances which make him guilty of an offence by divulging. It is wider in another respect: a dealing by a tippee as agent is covered by sub-section (3) though not, it seems, by section 75A of the *Securities Industry Act.*

In contrast with sub-sections (1) and (2), the prohibition imposed on the tippee by sub-section (3) of the Federal Bill can apply to a corporation. A corporation is associated with another person in the circumstances defined in section 14 of the Bill. Thus a corporation is associated with its director or employee, or with a director or employee, of a related corporation. Where a corporation is in possession of information obtained from such a director or employee the prohibition in sub-section (3) may apply to the corporation. The sub-section thus calls for an answer to the question of when a corporation is in possession of information. The general law on this question is discussed by Professor Gower.[12] He refers to a number of criminal cases and then says: 'In none of these criminal cases was (the) "organic" theory referred to in the judgments. But it seems clear that they were impliedly based on (the) view that certain officials are the company and not merely the agents of it. Indeed, in later decisions this has become explicit, and a limitation has been put on the ambit of the doctrine by making it clear that it is not the act or knowledge of every agent or servant of the company which will be attributed to the company, but only those who the company has made its "responsible officers" for the action in question. Moreover it appears that the courts will conduct a factual analysis of the workings of the company's management to discover who those officials are'.

The word 'then' in section 123(3) would appear to put the tippee in the same position as the person precluded under sub-section (1)

12 Gower COMPANY LAW 3rd ed. 147.

or (2) so far as time limits are concerned. Whenever he may have received the tip, he may use it with impunity if the person from whom he received it has by lapse of time ceased to be precluded by subsction (1) or (2) from himself dealing.

The Ontario *Securities Act* may impose a prohibition on a tippee, not because he has obtained information from an insider, but because he is an associate of an insider. Section 113 prohibits an associate of an insider from making use of specific confidential information. 'Associate' is widely defined in section 1(2).

The United States *Draft Securities Code* may impose a wider prohibition on a tippee than does section 121(3) of the Federal Bill. Section 1303 (b) of the *Securities Code* defines 'insider' so that it means

> '(1) the issuer, (2) a director, officer, parent, subsidiary, or sister company of the issuer, (3) a person whose relationship or former relationship to the issuer gives or gave him access to a fact of special significance about the issuer or the security that is not generally available, or (4) a person who learns such a fact from a person specified in this sub-section (including a person specified in this clause) with knowledge that the person from whom he learns the fact is such a person, unless the Commission or a court finds that it would be inequitable, on consideration of the circumstances and the purposes of this Code (including the deterrent effect of liability), to treat the person specified in this clause as if he were specified in clause (1), (2), or (3)'.

The provision clearly would extend to an indirect tippee. There is no equivalent in the US Code of the qualifications in terms of association, or arrangement for the communication of information, which apply to section 123(3) of the Federal Bill.

(d) SECTION 123(4)

A person shall not, at any time when he is precluded by sub-section (1), (2), or (3) from dealing in any securities, cause or procure any other person to deal in those securities.

Section 123(4) follows generally the provisions of section 12(3) of the UK 1973 Bill. The United Kingdom Bill however used only the word 'procure' and not the phrase 'cause or procure'.

One who deals as agent for another 'deals' for purposes of subsections (1), (2) and (3) of the Federal Bill. The assumption of those provisions is, however, that a person who, not acting as agent, causes or procures another to deal, does not himself deal. Sub-section (4) is presumably intended to cover, for example, the case of a person who persuades a member of his family to deal, or instructs another to act as agent for a member of his family. A simple recommendation would

not, it seems, amount to a causing or procuring. This is the inference to be drawn from sub-section (5) considered more fully below. Sub-section (5) prohibits, in restricted circumstances, the communication of information to another when the person communicating knows that the other will make use of the information for purpose of dealing. If the words 'cause or procure' in sub-section (4) were held to include recommending, sub-section (4) would impose a wider prohibition on recommending than is imposed by sub-section (5) on communicating information.

Where a person in possession of information deals as agent for a company, the relevant prohibition is section 123(1). Where he instructs another person to act as agent for the company, or persuades the board of his company or another officer to instruct another person to act as agent for the company, section 123(4) would appear to be the relevant provision. Section 123(4) may give rise to a logical difficulty if the prospect of a dealing by a company in the shares of another, as a preliminary to or in the implementation of a take-over bid, amounts to information which if generally known would be likely to affect materially the price of securities of the other company. Action by an officer of the first company to move the company to engage in the dealing would appear to be prohibited by the combination of section 123(2) and section 123(4). The officer is in possession of the material information that the company will deal; he cannot cause or procure the company to deal. A similar logical difficulty may arise from the combination of section 123(2) and s 123(6), considered hereafter, so that the company is precluded from dealing preliminary to making the take-over bid. The logical difficulties are overcome by sub-section 14(4) of the United Kingdom 1973 Bill. But there is no equivalent provision in the Federal Bill.

Section 123(4) overcomes what might be thought a significant omission in the provisions of section 75A of the New South Wales *Securities Industry Act*. Neither the Ontario *Securities Act*, nor the United States *Draft Securities Code* would appear to extend to the situations to which section 123(4) applies.

(e) SECTION 123(5)

A person shall not, at any time when he is precluded by sub-section (1), (2) or (3) from dealing in any securities by reason of of his being in possession of any information, communicate that information to any other person if—

(a) A registered stock exchange permits trading of those securities on the stock market maintained or provided by that stock exchange and

> *(b) he knows, or has reasonable grounds for believing that the other person will make use of the information for the purpose of dealing, or causing or procuring another person to deal, in those securities.*

Section 123(5) follows, generally, the section 12(4) of the United Kingdom 1973 Bill.

Section 123(5) prohibits tipping but, it will be seen, the only sanction is criminal proceedings. No civil liability is attracted by tipping. The prohibition is limited in that it applies only if trading in the securities is permitted on a stock exchange, and only if the person who communicates information knows or has reasonable grounds for believing that the person to whom he communicates will make use of the information for the purpose of dealing, or cause or procure another person to deal in those securities. Communicating information is the correlative of obtaining information which, in turn, is an element of the prohibition on dealing by a tippee under section 123(3). The prohibition by section 123(5) may operate where the tippee is not subject to a prohibition—because, for example, he is not associated with a tipper and has no arrangement with the tipper for the communication of information. Conversely a tippee may be liable under section 123(5) though his tipper is not subject to the prohibition imposed by section 123(5). The tipper may have reasonably believed that the tippee would not make use of the information. The tippee may be a relative of the tipper who knows that the tipper is himself precluded from dealing.

Some attention has already been directed to the distinctions which section 123(4) and section 123(5) seem to require between causing or procuring and communicating information, and between either of these and a simple recommending, which is neither a causing or procuring nor a communicating of information.

The Ontario *Securities Code* does not prohibit tipping, though it will impose liability on an associate of an insider who makes use of information which he may have received by way of a tip from an insider.

The United States *Draft Securities Code* does not prohibit tipping, but the effect of section 1419(c) is to impose, in some circumstances, a civil liability on a tipper co-extensive with the liability of a tippee. Section 1419 provides:

> 'An insider within section 1303(b) (1), (2), (3) inclusive (herein a "tipper") who discloses to an insider within section 1303(b) (4) (herein a "tippee"), or a tippee who discloses to another

tippee, a material fact that is not generally available is liable under (the sections imposing civil liability on insiders and tippees who deal) to the same extent as a tippee who is liable under either of those sections, unless he (1) disclosed the fact for a proper purpose and in a proper manner and (2) exercised reasonable care under the circumstances to assure that his tippee would not use the fact so as to become so liable'.

(f) SECTION 123(6)

Without prejudice to sub-section (3), a corporation shall not deal in any securities at a time when any officer of that corporation is precluded by sub-section (1), (2), or (3) from dealing in those securities.

Section 123(6) follows, generally, the provisions of section 12(6) of the UK 1973 Bill.

This prohibition, it will be seen, gives rise only to criminal proceedings. It is intended to be the principal control of insider trading by a corporation, though a corporation which is a tippee may be prohibited from dealing by section 123(3), and from causing or procuring by section 123(4). It has been noted that a corporation is not prohibited by section 123(1) or (2).

Section 123(6) is extraordinarily wide in its operation. A life insurance company is in theory precluded from dealing because a junior employee has recieved a tip which makes him subject to the s. 123(3) prohibition, and this notwithstanding that the junior employee has kept the tip to himself and has not in any way influenced the decision of the life company to deal. A corporation may be precluded from dealing because one of its non-executive directors has information notwithstanding that the director has not influenced the decision to deal and there are arrangements to ensure that he does not. A corporation engaged in portfolio management on behalf of clients may be precluded from dealing because some officers of the corporation have information as a result of an underwriting operation, and again notwithstanding that the officers with information have not influenced the portfolio management decision. In other respects, however, s. 123(6) is too narrow in its operation. It does not extend to the case where the dealing is by one corporation and that dealing has been influenced by an officer of a related corporation who has the information. The subsection will simply encourage the formation of a separate corporation to engage in dealing. Officers of the principal corporation who have information will give advice to officers of the separate corporation but will not communicate information to them. This is not

causing or procuring and no officer of the separate corporation will have the information.

It would, I suggest, be more appropriate to drop subsection (6) and, in its stead, include provisions which will:

(i) widen the operation of subsection (4) so as to include in the notion of causing or procuring the giving of advice by an officer of a corporation to another officer of the same corporation, or to an officer of a related corporation, where there is a dealing by the corporation or by the related corporation in the securities which are the subject of the advice; and

(ii) deem a corporation to be in possession of information and to have obtained that information in the manner defined in subsection (3) whenever it is shown that an officer of that corporation, or of a related corporation, who was in possession of information has, in the widened sense of the words, caused or procured the corporation to deal.

Section 75A of the NSW *Securities Industry Act* is inadequate to handle dealings through companies. There are no express provisions like section 123(6) in either the Ontario *Securities Act* or the United States *Draft Securities Code*. Comment 5(d) on section 1303 of the Code includes the following: ' . . . Nothing in the Code affects the question whether undisclosed information learned by an agent of a corporate "person" (for example, a bank) is attributed to the corporation and its other agents. The question of the efficacy of intra-corporate "Chinese walls" is thus left to the courts.'

(g) SECTION 124(1)

A person shall not deal in any securities of a prescribed corporation if he is in possession of information that is not generally available but, if it were, would be likely materially to affect the price of those securities and that information was obtained by him—

(a) in his capacity as a person holding office under or employed by Australia, a State or the Administration of a Territory; or

(b) in his capacity as a person in whom any functions are vested by a law of Australia or of a State or Territory or as a member of or person employed by an authority in which any functions are so vested.

Section 124(2) is intended to make sections 123(3), (4) and (5) applicable as if the person holding the office or employment or the functions referred to in section 124(1) were a person described by

section 123(1) or (2). The provisions of section 124(1) and (2) follow generally section 13 of the United Kingdom 1973 Bill.

Section 124 closes a gap which may be left by law and regulations applicable to persons holding offices or employments in public service, and extends prohibitions to tippees of such persons. There are no comparable provisions in the New South Wales law, or in the Ontario law or in the US *Draft Securities Code.*

(h) Exceptions relating to holders of dealers' licences

Sub-section (8) qualifies the operation of the other privisions of section 123. It provides that

> *(Section 123) does not preclude the holder of a dealers licence from dealing in shares, or units of shares, in a corporation, being shares or units that are permitted by a registered stock exchange to be traded on the stock market maintained or provided by that stock exchange, if—*
>
> *(a) the holder of the licence enters into the transaction concerned as agent for another person in pursuance of a specific instruction by that other person to effect that transaction;*
> *(b) the holder of the licence has not given any advice to the other person in relation to dealing in shares, or units of shares, of that class in that corporation; and*
> *(c) the other person is not associated with the holder of the licence.*

The effect of section 106(2) is that a person who acts as agent nonetheless deals in securities for the purposes of section 123. The combination of section 106(2) with section 123(6) (which, it will be recalled, provides that a corporation shall not deal in any securities at a time when any officer of that corportation is precluded by sub-section (1), (2), or (3) from dealing in those securities) is to create acute difficulty for any company engaged in portfolio management. There will be a liability on the corporation even though steps have been taken to set up a 'Chinese wall' between the officer who is concerned with the management of portfolios and any other officer who may have the information which under sub-section (1), (2) or (3) precludes him from dealing.

The United Kingdom Bill is much more liberal in the exceptions made to the operation of the provisions of that Bill equivalent to section 123 of the Federal Bill. Sub-section (8) of section 123 of the Federal Bill has its equivalent in section 14(2) (c) of the United Kingdom Bill: the latter provides that a person is not precluded from entering into transaction if he enters into the transaction as agent for another and has neither selected nor advised on

the selection of the securities to which the transaction relates. The exception is wider than the Australian sub-section (8). Where a broker who has information does give advice to a client, it may be that this should be treated in the way I have proposed in relation to advice given by an officer to his corporation or to a related corporation. I have a cutting from the London *Times* in which the financial editor commenting on the United Kingdom Bill suggests that a favoured client who has been given advice by a broker, who he knows or suspects has information, should be careful to deal through another broker.

And there may be yet other cases where advice should be treated in the way I have proposed. As the Bill now stands neither husband nor wife breaches any prohibition if the husband who has inside information gives advice to his wife on which she acts—it may be no more than a hint at the breakfast table.

There is an exemption in the United Kingdom Bill to allow a company engaged in portfolio management to select or advise on the selection of securities when information is possessed by one or more of its officers. Section 14(3) of the United Kingdom Bill provides:

> 'A company shall not be precluded by (being in possession of information as a tippee or by the fact that a director or officer of the company is precluded from dealing) from entering into any transaction by reason only of, or of having obtained, any information in the possession of a director or employee of the company if—
>
> (a) the decision to enter into the transaction was taken on its behalf by a person other than the director or employee; and
>
> (b) arrangements were then in existence for securing that the information was not communicated to that person and that no advice with respect to the transaction was given to him by a person in possession of the information; and
>
> (c) the information was not in fact so communicated and advice was not in fact so given.'

Under the Federal Bill, it has been seen, it is not possible for a company to escape the prohibitions of sub-section (3) and sub-section (6) of section 123 by setting up a 'Chinese wall' between the officers with information and those engaged in the portfolio management. Some exception to allow an appropriate escape should, it is considered, be included in the Federal Bill. But the suggestion made above in relation to sub-section (6) of section 123 may be more appropriate than adopting the United Kingdom exception. As the Federal Bill now stands, it will be necessary for a banker engaged in

portfolio management to set up a separate company to carry on this function, in which case something less than a 'Chinese wall' between the officers of the company engaged in portfolio management and officers of the old company will be effective to prevent liability of the portfolio management company under sub-section (3) of sub-section (6). The wall will not need to be proof against the movement of advice to the portfolio management company.

The United Kingdom Bill has a number of other exceptions. Most important, perhaps, is that in section 14(1) to which reference has already been made: A person is not precluded from entering into any transaction if his purpose is not, or is not primarily, the making of a profit or the avoiding of a loss, whether for himself or another. In the result intention to profit or to avoid a loss is a necessary element of insider trading transactions. Ontario law also requires an element of intention to gain. Other exceptions provided for in section 14(2) of the United Kingdom Bill have the effect that a person is not precluded from entering into a transaction if:

> (a) his sole purpose is the acquisition of qualification shares required by him as director or intending director of any company;
> (b) he enters into the transaction in pursuance of a scheme approved under Schedule 12 to the *Finance Act* 1972 (UK) (share option and share incentive schemes);
> . . .
> (d) he enters into the transaction in the bona fide performance of an underwriting agreement with respect to the securities to which the transaction relates;
> (e) he enters into the transaction in the bona fide exercise of his functions as trustee of a pension fund established wholly or primarily for the benefit of employees of the company to whose securities the transaction relates or of a related company; or
> (f) he enters into the transaction in the bona fide exercise of his functions as personal representative, liquidator, receiver or trustee in bankruptcy.

Paragraph (a) of section 14 (2) of the UK Bill may be unnecessary in view of the general provision in section 14(1) to which reference has already been made. Under the Federal Bill there is no equivalent of either provision, with the result that a director will on occasions be unable to comply with the articles in regard to qualification shares, except at the cost of committing an offence under section 123.

Paragraph (b) of section 14(2) of the UK Bill may protect an officer in the circumstances which in *Texas Gulf Sulphur* were held to involve a breach of Rule 10(b) (5). It may be thought that the

exception is unnecessarily wide. No corresponding exception is provided in the Federal Bill, though in most instances the officer will be able to raise the defence provided for in section 125(6) considered below. In any case, it is not clear under the Federal Bill that the taking up of an option issued by the company is a dealing, and some share incentive schemes may thus be outside the operation of section 123. It is true that the definition of 'dealing' in section 106(2) extends to subscribing for shares, so that the exercise of an option is a dealing, but at the time of exercise the information on which the officer acted in taking up the options may long since have become generally available.

Paragraph (e) of section 14(2) of the United Kingdom Bill may be unnecessarily wide. It is not difficult to set up a pension fund for the benefit of employees and the trustees '*bona fide* exercise of his functions' may very well require him to exploit information. The need for any exemption such as sub-paragraph (e) is not compelling. The United Kingdom Labour Government Green Paper directed criticism to paragraph (e).

Paragraph (f) of section 14(2) of the United Kingdom Bill would appear to provide an appropriate exception.

(i) *Criminal and Civil Proceedings*

Contravention of any provision of section 123 or section 124 of the Federal Bill is an offence. The penalty, in the case of a person who is not a corporation, is a fine not exceeding $10,000 or imprisonment for a term not exceeding two years. The United Kingdom Bill is more Draconian in providing a maximum penalty for seven years. If the person is a corporation, the penalty is a fine not exceeding $50,000.

Contravention of many of the provisions of section 123 and 124 also involve civil liability. The provisions which, exceptionally, do not give rise to civil liability are section 123(5)—tipping—and section 123(6)—corporate dealing when an officer is precluded.

The fact that every prohibition is sanctioned by criminal proceedings is in sharp contrast with the approach of the Ontario law which relies entirely on civil proceedings. The US *Draft Securities Code* does provide for criminal proceedings, but not however in relation to all prohibitions. Thus the tipper in the United States is subject only to civil proceedings.

A defence to both criminal and civil proceedings is provided by section 125(6) of the Federal Bill. Where a prosecution is instituted against a person for an offence, or an action is brought against a person,

by reason that the person has entered into a transaction in contravention of section 123 or 124, it is a defence if the person satisfies the Court that the other party to the transaction knew, or ought reasonably to have known, of the information before entering into the transaction.

There is no equivalent defence available under the United Kingdom Bill. The US *Draft Securities Code* section 1303, defines the conduct which is unlawful so as to exclude a transaction if (1) the insider believes, and has reasonable ground to believe, that the fact is generally available or (2), if the other party to the transaction (or his agent) is identified, (a) the insider believes, and has reasonable ground to believe that that person knows it, or (b) that person in fact knows it from the insider or otherwise. This exclusion clearly has a wider operation than the defence provided for by section 125(6) of the Federal Bill.

By section 125(5) of the Federal Bill the liability of a person who deals or causes or procures another person to deal in contravention of those provisions of sections 123 and 124 which give rise to civil liability is to compensate any other party to the transaction who was not in possession of the information, for any loss sustained by that person by reason of any difference beween the price at which the securities were dealt in and their likely price if that information had been generally available. The liability is to compensate only a person who was not in possession of the information. The defence to an action provided for in sub-section (6) that the other party *knew* of the information is thus, in this context, unnecessary.

The assessment of damages requires the determination of the likely price of the securities at the time of the transaction, had the information been generally available. Where the transaction which is the subject of the action is in respect of securities which are not permitted by any registered stock exchange to be traded on the stock market maintained by that stock exchange 'generally available' means 'not available to all parties to the transaction' and 'likely price' is the price at which the securities would have been dealt in had the information been available to all parties to the transaction. At least this would appear to be the intention of section 106(2), though it does not expressly extend the constructions to include references in section 123(5).

Where the securities are permitted to be traded on a stock exchange, and the transaction has in fact been concluded on the exchange, the action for damages is not of any practical significance since the plaintiff will not, save in a rare case, be able to show that he entered into

a transaction to which the defendant was a party or which the defendant had caused or procured. Such a transaction is sometimes referred to as 'faceless'. Stock exchange and broking procedures do not generally admit of identifying the parties to a particular transaction. Where in any instance identification is possible, the matching of the seller and the buyer will in any case be fortuitous and one might think that a right of action in the person who has dealt with the insider is inappropriate. Nonetheless the United Kingdom Labour Party Green Paper proposes that there be changes in stock exchange practices that would enable the parties to a transaction to be identified.

Where the transaction is off-market, and is therefore face-to-face, the action for damages if of practical significance and the assessment of damages will presumably involve a determination of what the price on the stock exchange would have been at the time of the transaction had the information been generally available. The price of the securities on the exchange after the subsequent disclosure of the information may provide some hindsight, but it will not necessarily fix the likely price for purposes of the assessment of damages.

Where the transaction relates to securities not permitted to be traded on a stock exchange, 'determining the likely price' involves a conclusion as to what the parties would have agreed as the price at which the securities would be sold had the information been available to all parties to the transaction.

Section 125(5) presumably deems the plaintiff to have suffered a loss as measured by the difference between the price he paid or was paid and the likely price. The fact that he has resold the securities he bought, or has bought others in substitution for those he had sold, and may thus in fact not have suffered any loss, is on this sssumption irrelevant.

The Ontario law gives an action for damages but it does not attempt to define the measure of damages. The United States *Draft Securities Code* has a number of provisions relating to an action for compensation. They overcome the problems of the plaintiff who has entered into a 'faceless' transaction at a time when a person was making a prohibited dealing. And they make more elaborate provisions than the Federal Bill in regard to the assessment of damages. Section 1402(b) of the *Draft Code* provides that 'if the transaction is effected in a manner that would make the matching of buyers and sellers substantially fortuitous, a seller or buyer who violates (the prohibition on insider dealing in section 1303(a)) is liable for damages to a person who buys or sells between (1) the day when the defendant

first unlawfully sells or buys and (2) the day when all . . . facts of special significance . . . become generally available . . . ' The possible astronomical liability to which a provision of this kind could give rise where there has been a substantial volume of dealings on the market during the relevant period is avoided by section 1402(f) which limits the measure of damages by reference to the amount of securities that the defendant bought or sold. There are provisions in section 1409 for pro-rating damages among all actual and potential plaintiffs. In the result, where there has been a substantial volume of dealings on the market during the relevant period, an individual plaintiff will very likely recover no more than a small amount.

If civil liability is to be made significant under the Federal law where transactions are 'faceless', some such provisions as those of the US *Draft Code* will be necessary. And it will also be necessary to provide procedures by which all potential plaintiffs may recover without risk in relation to costs. In his memorandum for the Australian Government on Proposals for an Australian Securities Legislation, Professor Loss suggested that the Federal Securities and Exchange Commission should be authorised, or perhaps even directed in appropriate cases, to bring actions looking towards restitution to the insider's victims. The Bill, as at present drafted, does not act on that suggestion. Even if the model of section 1409 of the US *Draft Securities Code* were adopted, the civil action available to the party to a 'faceless' transaction would still lack practical significance. No one plaintiff would be prepared to take the risk of costs if the action fails. The contingent fees system which prevails in the United States and the fact that costs, other than court fees, are not in general awarded against a plaintiff, are important differences between United States and Australian procedures.

The measure of damages under the US *Draft Code,* section 1402, gives greater significance to the price of the securities at the time when information becomes generally known than does the Federal Bill, and it seeks to confine the plaintiff to his actual loss where he has resold, or bought substitute securities, before the information becomes generally available.

The Federal Bill does not contain any provisions giving a civil action to the company in whose securities the insider has dealt. In this way, the problem of correlating the recovery of damages by the person who has bought or sold with the company's recovery, so as to prevent double recovery, is avoided. Obviously it is preferable to give a remedy to the person who has suffered loss. Recovery by the com-

pany will enure to the benefit of the defendants so far as they are shareholders, unless the company recovers as trustee for those who have suffered loss. In the *Texas Gulf Sulphur Case,* on remand to Bonsal J, it was ordered that the company should recover the gains made by insiders and that the company should hold the amount recovered in escrow, presumably for the benefit of those who had dealt at the time the insiders were dealing on the market. Proceedings in that case were taken by the Securities and Exchange Commission. Recovery by the company could not in Australia be relied on as the method of ensuring compensation to those who have suffered loss without some radical new provisions giving persons who have dealt with insiders access to the amount recovered by the company, and provisions whereby the Corporations and Exchange Commission would be authorised, or perhaps required, to bring proceedings on behalf of the company. Under the present Australian law a shareholder may in effect institute proceedings by the company, by way of a derivative suit. But the consequences in liability for costs, if unsuccessful, make this only a theoretical possibility.

The US *Draft Code* has preserved the company's action to recover short-swing profits from insider transactions presently provided for in section 16(a) of the *Securities Exchange Act* of 1934. The relevant provision is section 1413 of the *Draft Securities Code.* The impression is conveyed by the Reporter's Notes to this section of the *Draft Code* that he considers an effective remedy is available to those who have suffered loss and this may make section 1413 unnecessary. Meanwhile the *Draft Code* includes other provisions (section 1413 (i)) which will overcome the possibility of double recovery—by the company under section 1413 and by the person who suffered loss under section 1402.

Despite the problem of possible double recovery, both the United Kingdom White Paper and the Green Paper favour an action by the company in addition to actions available to those who have suffered loss.

(3) *The Relationship of the Bill to State Law*

Section 18 of the Federal Bill pronounces that it is the intention of Parliament that the provisions of the Act should operate to the exclusion of any provision of the law of a State or Territory that deals with a matter dealt with by the Federal provisions. So far as insider trading provisions are concerned this pronouncement is, however,

nullified by section 125(7) which provides that nothing in the section affects any liability that a person may incur under any other law.

Attention was drawn in Part I of this article to the attempts by section 124(2) of the New South Wales *Companies Act* and section 75A of the *Securities Industry Act* to set the spheres of operation of those provisions and to prevent double recovery. It is not by any means certain that they have been successful: the correlation between the company's action under section 75A and of the action under that section by a person who has suffered loss is obscure. And there are possibilities of actions by the company under the general law expressed in *Regal v Gulliver*[13] and *Boardman v Phipps*,[14] and by a person who has suffered loss if he can overcome *Percival v Wright*.[15]

It is not intended in this article to attempt to show how those problems of correlation or the further problems arising from the concurrent Federal provisions might be resolved. It is enough to observe that the Bill will multiply problems of correlation.

R W PARSONS*

13 [1942] All ER 378.
14 [1967] 2 AC 46.
15 [1902] 2 Ch 421.

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APPENDIX

The key provisions of the Ontario *Securities Act* 1966 (as amended) are as follows:

SECTION 1 (1) . . .

2. 'Associate', where used to indicate a relationship with any person or company, means,
   i. any company of which such person or company beneficially owns, directly or indirectly, equity shares carrying more than 10 per cent of the voting rights attached to all equity shares of the company for the time being outstanding,
   ii. any partners of that person or company acting by or for the partnership of which they are both partners,
   iii. any trust or estate in which such person or company has a substantial beneficial interest or as to which such person or company serves as trustee or in a similar capacity,
   iv. any spouse, son or daughter of that person, or
   v. any relative of such person or of his spouse, other than a relative referred to in subparagraph iv, who has the same home as such person.

   . . .

28. 'senior officer' means,
   i. the chairman or any vice-chairman of the board of directors, the president, any vice-president, the secretary, the treasurer or the general manager of a company or any other individual who performs functions for the company similar to those normally performed by an individual occuping any such office, and
   ii. each of the five highest paid employees of a company, including any individual referred to in subparagraph i.

   . . .

SECTION 109 (1)

. . .

(*c*) 'insider' or 'insider of a corporation' means,
   (i) any director or senior officer of a corporation,
   (ii) any person or company who beneficially owns, directly or indirectly, equity shares of a corporation carrying more than 10 per cent of the voting rights attached to all equity shares of the corporation for the time being outstanding, provided that in computing the percentage of voting rights attached to equity shares owned by an underwriter there shall be excluded any equity shares that have been acquired by him as underwriter in the course of distribution to the public of such shares, but such exclusion ceases to have effect on completion or cessation of the distribution to the public by him, or
   (iii) any person or company who exercises control or direction over the equity shares of a corporation carrying more than 10 per cent of the voting rights attached to all equity shares of the corporation for the time being outstanding.

For the purposes of this Part,

(*a*) every director or senior officer of a company that is itself an insider of a corporation shall be deemed to be an insider of such corporation;

(*b*) the acquisition or disposition by an insider of a put, call or other transferable option with respect to a capital security shall be deemed a change in the beneficial ownership of the capital security to which such transferable option relates; and . . .

SECTION 110 (1)

A person or company that becomes an insider of a corporation shall, within ten days after the end of the month in which he becomes an insider, file with the Commission a report as of the day on which he became an insider, of his direct or indirect beneficial ownership of or control or direction over capital securities of the corporation.

. . .

SECTION 110 (3)

A person or company that has filed or is required to file a report under this section or any predecessor thereof and whose direct or indirect beneficial ownership of or control or direction over capital securities of the corporation changes from that shown or required to be shown in such report or in the latest report filed by him under this section or any predecessor thereof shall, within ten day following the end of the month in which such change takes place, if he was an insider of the corporation at any time during such month, file with the Commission a report of his direct or indirect beneficial ownership of or his control or direction over capital securities of the corporation at the end of such month, and the change or changes therein that occurred during the month giving such details as may be required by the regulations.

. . .

SECTION 111 (1)

All reports filed with the Commission under section 110 . . . shall be open to public inspection at the offices of the Commission during normal business hours of the commission, and any person may make extracts from such reports.

SECTION 111 (2)

The Commission shall summarize in or as part of a monthly periodical for distribution to the public on payment of a reasonable fee therefor the information contained in the reports so filed.

. . .

SECTION 113 (1)

Every insider of a corporation or associate or affiliate of such insider, who, in connection with a transaction relating to the capital securities of the corporation, makes use of any specific confidential information for his own benefit or advantage that, if generally known, might reasonably be expected to affect materially the value of such securities, is liable to compensate any person or company for any direct loss suffered by such person or company as a result of such transaction, unless such information was known or ought reasonably to have been known to such person or company at the time of such transaction, and is also accountable to the corporation for any direct benefit or advantage received or receivable by such insider, associate or affiliate, as the case may be, as a result of such transaction.

SECTION 113 (2)

An action to enforce any right created by subsection 1 may be commenced only within two years after the date of completion of the transaction that gave rise to the cause of action.

SECTION 114 (1)

Upon application by any person or company that was at the time of a transaction referred to in subsection 1 of section 113 or is at the time of the application an owner of capital securities of the corporation, a judge of the High Court designated by the Chief Justice of the High Court may, if satisfied that,

(*a*) such person or company has reasonable grounds for believing that the corporation has a cause of action under section 113; and

(*b*) either,

(i) the corporation has refused or failed to commence an action under section 113 within sixty days after receipt of a written request from such person or company so to do; or

(ii) the corporation has failed to prosecute diligently an action commenced by it under section 113,

make an order, upon such terms as to security for costs and otherwise as to the judge seems fit, requiring the Commission to commence or continue an action in the name of and on behalf of the corporation to enforce the liability created by section 113.

SECTION 114 (2)

The corporation and the Commission shall be given notice of any application under subsection 1 and has the right to appear and be heard thereon.

SECTION 114 (3)

Every order made under subsection 1 shall provide that the corporation shall co-operate fully with the Commission in the institution and presecution of such action and shall make available to the Commission all books, records, documents and other material or information known to the corporation or reasonably ascertainable by the corporation relevant to such action.

. . .

NOTE:

Similar provisions are contained in the Ontario *Business Corporations Act*. The *Securities Act* provisions apply to insiders of a corporation as defined in Part X of that Act—broadly a company which has issued equity shares distributed to the public or any of whose shares are listed on a recognized stock exchange. The *Business Corporations Act* provisions apply to insiders of a corporation that is offering its securities to the public.