KAMPALA INTERNATIONAL UNIVERSITY

SCHOOL OF LAW

AN ANALYSIS OF THE LAW AGAINST INSIDER TRADING IN UGANDAN CAPITAL MARKET

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DECLARATION

I hereby declare that except for references to other peoples work, which have been duly acknowledged, the study presented here was written by me, under the supervision of Dr.Adenyuma Gabriel. It is a record of my own research work and has not previously been presented in any form whatsoever in any application for a degree elsewhere. All sources of information collected and materials used have been duly acknowledged by means of references.

STUDENT

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SIGNATURE

.....

DATE

25th/10/2018

APPROVAL

I have approved the mentioned final year report to be presented as a partial requirement for the acquisition of Bachelor of Laws at Kampala International University

(SUPERVISOR)

DR. ADENYUMA GABRIEL

SIGNATURE

.....

DATE

.....26/10/18.....

DEDICATION

I dedicate this work primarily to the almighty God for his guidance and mercy throughout my studies. I also dedicate this work to my Late Dad Mr. EnoMusungwe and Mother Enid MusungweBiirafor the support, love and care they have given me throughout my studies.

ACKNOWLEDGEMENT

I wish to thank the almighty God for giving me the strength and courage to pursue this project. Let me also acknowledge the immense support and assistance rendered by my supervisor Dr.Adenyuma Gabriel who was available at all times to guide me throughout the project.

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LIST OF ACRONYMS

AMEX-American Stock Exchange

CCMAA-Capital Markets Authority Act

CMA-Capital Markets Authority (CMA)

EDGAR-Electronic Data Gathering, Analysis and Retrieval

EU-European Union

IOSCO-International Organization of Securities Commission

LSE-London Stock Exchange

NASDAQ-National Association of Securities Dealers Automated Quotations

NYSE -New York Stock Exchange

SEC-Security Exchange Commission

SROs-Self-Regulatory Organizations

USA-United States of America

LIST OF STATUTES

The Capital Markets Authority Act Cap 84

The Capital Markets Authority(Amendment) Act 2011

The capital Markets Authority (Amendment) Act 2016

Capital Markets (Asset Backed Securities) Regulations, 2012 statutory instruments 2012 No. 46.

The Capital Markets (Cross Border Introductions) Regulations, 2004(2004 No. 43)

Uganda Securities Exchange Limited Insider Trading Rules 2008

LIST OF CASES

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ABSTRACT

As the world continues to expand in global markets, trading of shares, bonds, derivatives and other instruments continue to increase. One form of trading that has received considerable interest in recent years is insider trading. In order to protect the integrity of the market and to combat market abuse in the Ugandan Capital markets, the Capital markets Authority Act, the subsequent establishment of the Ugandan securities Exchange in 1997 and Insider Trading Rules were enacted prohibiting the dealing of securities of a listed company by an insider of that company which brought some confidence in the capital market. The provisions of Capital markets Authority Act were to some extent inadequate and ineffectively implemented and eventually the Act was amended to overcome the flawed provisions. It is against this background that an analysis of the legal and regulatory framework of market abuse and insider trading is carried out to expose the flaws that were previously embedded in Uganda market abuse laws. This is done to raise awareness of the situation on the part of the relevant stakeholders. To this end, this research is a conceptual study of the provisions of the Act prohibiting insider trading, and the Ugandan Securities Exchange Insider Trading Rules, 2008, analyzing the goal of preventing insider trading and to recommend possible regulatory measures that could be incorporated in the Uganda market abuse regime not only to bridge the gaps for a more comprehensive approach on insider trading but also to further increase investor confidence in Uganda's stock exchange.

CHAPTERISATION

The aims of this research paper are stated in the abstract. Although the literature on insider trading is too voluminous to cite in detail, there is little literature on insider trading in Uganda. Students, professionals and prospective investors who may need to know more about insider trading in Ugandan capital Markets will find research useful.

The format of this research is different from the most researches. The researcher has prefaced each chapter with a textual introduction, explaining the topic under discussion. The materials referred to in the research text then appear as footnote at the end of each page as well as bibliography at the end of the research. The hope is the reader can gain an overview of the topic in question and then build on that reference to the materials. It should also provide a useful tool for final revision.

Needless to say, but I will, this research is but a halfway house to achieving the reader' aims. Thus readers should look to read the materials referred to in their entirety whenever possible. There is voluminous literature on insider trading and these should obviously be used in conjunction with this research.

Chapter 1 is a general introduction to the subject of insider trading. It lays out the introduction, background to the study. It also outlines the objectives, purpose and scope of the study. It discusses the methodology adopted by the researcher and importantly, reviews literature on insider trading both within and outside Uganda.

Chapter 2 looks at the history of insider trading. The history of insider trading, contains extracts from excellent essays on aspects of the historical background to insider trading and its development. It looks at United States and United Kingdom insider trading system. This is because United States has historically been the world leader in insider trading law. This Chapter also discusses the meaning of insider trading. It also discusses what amounts to an insider, insider information, material and immaterial information. Within this context, the point when information is deemed public or non-public is discussed. Finally, the chapter discusses the meaning of Capital markets.

Chapter 3 gives a background of insider trading laws and their progression in Uganda. It lays out the statutory text of the insider trading regulations of Uganda capital markets.

Chapter 4 analyses effectiveness of the legal framework of insider trading in Ugandan capita; markets

Finally in **Chapter 5,** the researcher notes the weaknesses in the insider trading legislation and recommends legislative intervention and possible regulatory measures that could be incorporated in the Ugandan market abuse regime.

CHAPTER ONE

1.0 Introduction

Insider trading is one of the categories of market misconduct under the Capital Markets Authority Act[1] and as a practice, it has been vilified because it is seen as a misappropriation of the company's property which includes information and it also entails an abuse of the directors' fiduciary duties.[2]Insider trading means the trading in organised securities markets by persons in possession of material non-public information.

This research paper is a conceptual study of the legal framework prohibiting insider trading in Ugandan capital markets and an evaluation of the adequacy of the legal framework in achieving the goal of preventing insider trading.

Insider trading has always been the stuff of controversy and scandal, making headlines and destroying reputation. It is at the very root of discrimination, as it gives a small, usually already relatively privileged minority an unfair advantage over the broad majority who do not enjoy the same equality of information or opportunity. The use of privileged information for the purposes of gain at the expense of others is morally and legally reprehensive. The eradication of this practice is essential to the efficient working and reputation of any markets, and the society in which it operates. It is also a non-negotiable requirement for all markets to remove any suspicion of impropriety in order to attract and retain investment flows.[3]Many people have been willing to look at insider trading as an issue that requires serious analytical work.[4]

1.1 Background

In a country whose aim is to promote and facilitate the development of an orderly, fair and efficient capital markets industry[5] and where secondary market in transferable securities plays an important role in the financing of economic agents there is no doubt that for the market to be able to play its role effectively, every measure should be taken to ensure that the market operates smoothly, the market should be seen to operate fairly and on the basis of equal information.[6] To this end, a range of procedures can be used to check company's compliance with the laws and regulations governing capital markets and the regulatory bodies should have wide powers to take corrective and punitive measures against the entities or

1 Chapter 84
2Chiarella-v-U.S., 445 U.S 222(1980)
3 Insider trading and other Market Abuses(Including the Effective Management of Price Sensitive Information at page 3
4 Henry G. Manne, Insider Trading and Property Rights in new Information at 933
5 Preamble to the Capital Markets Authority Act Cap 84
6Uganda Securities Exchange Limited Insider Trading Rules 2008, Rule 1

individuals involved in the violation of the laws, regulations and directivesand fixing personal liability on directors and officials of the companies for the severe violations of the law especially those who commit offences relating to trading in securities, promotion and floatation of securities and those that negatively affect the orderly, fair and efficient capital markets industry in Uganda.

1.2 Statement of the problem

Insider trading has been the interest for research for many authors, in particular, the effects of insider trading in the welfare and the functioning of the markets have been discussed and in an extent have not been totally clarified.[7]

Uganda was very slow in implementing rules against insider trading in comparison to other countries. The law that put such restrictions into force was passed as late as 1996, the Capital Markets Authority Act, the Uganda Securities Exchange Limited Insider Trading Rules, 2008 were enacted and the provisions of the Capital Markets Authority Act on insider trading were substantially amended in 2016. This research a conceptual study the laws prohibiting insider trading and evaluating their adequacy not only in preventing insider trading but also in protecting the integrity of the market.

There is a limited understanding of the concept of insider trading in Uganda and the persons who are insiders for the purposes of insider trading are not clear. There is also a misconception that all insider trading are illegal. The insider trading legal framework is wanting and some requirements of the law are not met by corporate bodies and directors thereof. There is limited literature on the subject of insider trading in Uganda. It is therefore the ripe time to synthesise the existing research focusing not only on expanding the literature but also to analyse the insider trading in Uganda.

1.3 Statement of Objectives

1. To examine the history of insider trading regulation in Uganda and the rationale for restrictions on insider trading.
2. To examine the legal framework regulating capital markets in Uganda.
3. To investigate and analyse the concept of insider trading in other jurisdictions both for the purposes of drawing analogies and for comparing and contrasting the subject of insider trading in other countries.

7 Merger Announcements and Insider Trading Activity. An Empirical Comparative Investigation in LSE and ASE

4. To find out what lessons can Uganda learn from other countries and to make viable recommendations for the effective regulation of insider trading in Ugandan capital markets

1.4 Research questions

1. What is the meaning and rationale of restrictions on insider trading in capital markets
2. What is insider information and who is an insider for purposes of insider trading
3. Are all insider trading illegal and who is injured as a result of insider trading
4. What lessons can Uganda learn from other jurisdictions as far as insider trading is concerned?
5. How is the existing legal framework affecting insider trading in Uganda.

1.5 Scope of the study

The study deals with the subject of insider trading in Ugandan capital markets. The study analyses the existing legal framework and for comparative purposes, reference will be made to the subject and practice of insider trading in other countries.

1.6 Significance of the study

1. The study will examine the legal framework regulating insider trading and capital markets in Uganda.
2. The study will examine the role of insider trading regulation in the promotion of economic growth in Uganda.
3. The results of the study will not only help us to compare the subject of insider trading as perceived and practiced in other jurisdictions but also the lessons that Uganda can learn from other jurisdictions
4. The study will analyse the challenges to the regulation of insider trading in Ugandan capital markets and recommendations will be proposed by the researcher as solutions to the challenges in order to protect the integrity of the market.

1.7 Methodology

The research basically applied doctrinal research methodology. This entailed reading background materials such as legal dictionaries and textbooks, locating primary materials including legislations and case law, analysing secondary sources of information which include academic writings on insider trading such as text books, law journals and scholarly articles and coming to a tentative conclusion.

1.8 Literature Review

Insider trading remains one of the most controversial aspects of securities regulation, evidenced by the growing body of literature which questions whether insider trading is even harmful, much less worthy of legal action.[8] The issue of insider trading has never disappeared from academic and public policy debates.[9] Academic analysis has considered insider trading from the perspectives of such diverse disciplines as economics,[10] Ethics,[11] feminist studies[12] and psychology.[13]

It has been said that if there is one fact which critics and proponents of insider trading dealings laws are certain to agree, it is that rules designed to prohibit trading on inside information are popular.[14] Virtually every country with a developed securities market has implemented legislation regulating insider dealing and in the vast majority cases, criminal sanctions have been imposed, Uganda not being an exception and has recently reaffirmed its policy commitment in the Capital Markets Authority Act.[15]

Insider trading has long been the subject of intense debate and more recently, intensive activity. Those arguing that insider trading should be prohibited state that it destroys investor confidence in the st0ck market and harms those who trade with, or on the other side of the market from, the insider.[16]

Opponents of insider trading also make two related, but mutually exclusive arguments; first that insider trading delays the release of information both to the public and within the corporate efficiency, and second, conversely, that it harms corporation's by resulting in the premature release, through leakage, of their confidential information.[17]

Those who argue that insider trading should not be prohibited and sometimes that it should actively be encouraged argue that it does not harm traders[18] and does not decrease confidence in the markets.[19] It is also argued that since insider trading does not harm anyone and

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8 Clark, Stephen Rhett. "Essays in insider trading, informational efficiency, and asset pricing." PhD (Doctor of Philosophy) thesis, University of Iowa, 2014 at page 1
9 Paula. J Dalley, From Horse Trading to Insider Trading Debate' 39 WM & MARY L. REV 1289(1998)
10 Henry G Manne, Insider Trading & Stock Market (1996), Javier Estrada, Insider Trading Regulation, Securities Markets and Welfare Under Risk Aversion' 35 Q. REV. ECON & FIN. 42
11 Ian B. Lee, "Fairness and Insider Trading" 2002, COLUM. BUS. L REV. 119
12 Judith G. Greenberg, "Insider Trading and Family Values" 4. WM.& MARY J WOMEN & L. 303 1998
13 John Dunkelberg & Debra Regin Jessup, "So then why did you do it? 29 J. BUS Ethics 51(2001)
14 Harry MC Vea, What's Wrong with Insider dealing? Legal Studies 15(1995)
15 Cap 84
16 Shapiro-v- Merrill Lynch Pierce, Fenner& Smith, Inc 495 F.2d 228 2 Cir. 1974
17 Scott, Insider Trading. Rule 10(b) -5, Disclosure and corporate Privacy, 9 J. LEG. STUD.801, 814-15 (1980)
18 Carney, Signalling and Causation in Insider Trading, 36 CATH. U.L REV. 863(1987)
19 Barbara Ann Banoff, The Regulation of Insider Trading in the United States, United Kingdom and Japan, at 146

produces substantial benefits, it is not unfair.[20] The researcher faults the author for asserting that insider trading does not harm anyone. It is the researcher's view that insider trading results in market manipulation in which the public has great interest. Public confidence in the fairness of markets enhances their liquidity and efficiency. Market manipulation harms the integrity of, and thereby undermines public confidence in securities and derivatives markets by distorting prices and creating an artificial appearance of market activity. It is the researcher's view that authorities around the world need to have adequate systems in place to detect, investigate and prosecute market manipulation.

While Daniel R. Fischel and Dennis W. Calton[21] reasonably argue that the literature on insider trading is too voluminous to cite in detail, there is little literature on insider trading in Uganda and in particular, in the banking industry.

The learned authors[22] state that the starting point for anyone interested in the subject of insider trading is *Henry Manne's* brilliant book, Insider Trading and the Stock Market,[23] which argues that insider trading is an efficient way to compensate entrepreneurs. Henry Manne argues and the researcher agrees, that insider trading compensates entrepreneurial achievements of insiders which would otherwise be unnecessary expense of the corporation. In support to this position, the researcher contends that the profits from insider trading constitute the only effective compensation scheme for entrepreneurial services in large corporations. While Manne made a strong economic case for insider trading, it is not unreasonable to criticise him. Thus Manne's arguments for insider trading may be faulted as follows; insider trading does not reward efficient management but generally reward possession of confidential inside information whether such information is favourable or not to the corporation's prospects. Insider trading leads to loss of efficiency due to the incentives that are created for the insider to conceal information or disseminate misinformation about the company while engaging in trading its securities.

Levmore[24] argued that insider trading creates perverse incentives by allowing corporate managers to profit on bad news as well as good and encourages managers to invest in risky projects. To this, the researcher agrees but hastens to add that insiders can rely on undisclosed company information both negative and positive information to make decisions. Where the

20 Easterbrook, Insider Trading, Secret Agents, Evidentially Privileges and Production of Information, 1981 SUP. CT. REV.309, 323-39
21 Daniel R. Fischel& Dennis W. Carlton, "The Regulation of Insider Trading," 35 Stanford Law Review 857 (1982) at 857
22 Daniel R. Fischel and Dennis W. Carlton
23 H. Manne, Insider Trading and the Stock Market passim (1966)
24Levmore, Securities and Secrets: Insider Trading and the Law of Contracts, 68 VA. L. REV. 117 (1982)

insider determines that he may make loss in any transaction, he does not enter into such transactions yet the outsider who is not in possession of such information can easily enter into such transactions to his or her detriment.

Haft has argued that insider trading impedes corporate decision making[25]and tempts managers to delay public disclosure of valuable information. To this, the researcher may only add that to permit insider trading there is a temptation for those responsible for ensuring prompt disclosure of price sensitive information to delay or manipulate the disclosure and the harm occasioned to the companies and public justifies legal liability.

Some also have argued that insider trading is an inefficient compensation scheme because, in effect, it compensates risk-averse managers with a benefit akin to lottery tickets.[26] Still others have claimed that insider trading allows insiders to divert part of the firm's earnings that would otherwise go to shareholders and therefore raises the firm's cost of capital.[27]

It has been stated that because insider trading has continued to thrive despite regulation, firms still have incentives to minimize the practice if prohibition were in the best interests of investors. The absence of widespread private restrictive measures even today beyond what is required by regulation is therefore difficult to reconcile with the general perception that insider trading is harmful to investors.[28] The researcher disagrees with the learned author. It is the researcher's view that to say the inadequacy of the statutory provisions and the efforts of the self-regulatory authorities is not to say that insider trading is not illegal or that it is approved.

According to the theory of market efficiency, no insider trading can occur and no trader can 'bit' the market. According to empirical evidence, however markets are not strongly efficient. In fact insider trading produces large and significant cumulative returns. More precisely, Meulbroek (1992) argued that trade specific characteristics lead to the incorporation of the insider trading into prices, offering to insiders great abnormal returns.

Moreover, Finnety (1976) argues that that insiders are able to outperform the market since they can and do in fact identify profitable as well as unprofitable situations within their

25Haft, The Effect of Insider Trading Rules on the Internal Efficiency of the Large Corporation, 80 MICH. L. REV. 1051 (1982)

13 Easterbrook, Insider Trading, supra note 1, at 332; Scott, supra note 1, at 8

27 Mendelson, Book Review, 117 U. PA. L. REV. 470 (1969) at 477-78.

28 Daniel R. Fischel& Dennis W. Carlton, "The Regulation of Insider Trading," 35 Stanford Law Review 857 (1982) at 859

corporations. In fact, the insiders gain from the fact that they sell stock following periods of positive abnormal returns and buy after periods of negative return.[29]

Inside trading has tremendous effects on the market in many ways. More precisely, according to Bernabou and Laroque (1992) many types of insiders have both the ability and the incentives to manipulate public information and asset prices through strategically distorted announcements or forecasts. They show that in the short run, inside trader can gain more by both speculation and spreading information and thus manipulating the market only if different agents follow one another in these positions and so learning remains incomplete leaving a constant scope for manipulation.[30]

Jimmy Walabekyi,[31] defined insider trading to mean trading in organized securities markets by persons in possession of material non-public information. It is one of the categories of market misconduct under the Capital Markets Authority Act Chapter 84 and as a practice, it has been vilified because it is seen as a misappropriation of the company's property, which includes its information, and it also an abuse of the directors' fiduciary duties. It also has an adverse effect on the company's reputation ,and the value of its securities, and on the whole it affects the public confidence in the capital markets of the country. Also, insider trading is seen as promoting unfairness on the securities exchange as all members of the investing public should be subject to identical market risks, but insider trading enables those who trade on the basis of inside information to bear less risks, compared to other investors who trade in the absence of this information. In recognition of these realities the stated purpose of the Uganda Securities Exchange Insider Trading Regulations, 2008 is to promote investor confidence, promote market efficiency, fairness and orderliness, and to assure investors that they will be protected against the use of inside information. However, in favor of insider trading, it has been argued that it encourages insiders to gather information, that will trickle through to the rest of the capital markets and rewards corporate insiders for their efforts. That notwithstanding, it is the opinion of the author that the advantages of insider trading regulation far outweigh the disadvantages, so it should remain prohibited by law. The author defined Insider Trading to involve dealing in securities of a company by an insider on the basis of non-public information that has a material effect on the price of securities.

29Meger Announcement and Insider Trading Activity. An Empirical Comparative Investigation in LSE and ASE at 2
30 ibid
31 Jimmy Walabyeki, Insider Trading in Uganda: Analysis of the Capital Markets Regulatory Framework at 1

With respect to banking industry, it has been argued, and the researcher agrees that reputation is an important issue among investment bankers and the investment banking industry is subject to a rigid hierarchy that ties an investment bank's reputation to its influence in the industry.[32] The investment banks in the upper bracket of the hierarchy enjoy a more prestigious and lucrative position than their counterparts in the lower bracket and the investment banks would aggressively defend their place in the hierarchy, even pulling out of profitable deals.

The lawsuits about the losses suffered by some major companies in trading financial derivatives under the advice of their investment bankers tarnish the reputation of the investment banking industry. Reputation being so important in the investment banking industry, it becomes a surprise to observe systematic activities that undermine the public's confidence in the industry. The effectiveness of the firm reputation restrains members of the investment banking industry from systematically exploiting their superior information regarding their own firms. In this regard, the researcher contends that insider trading harms the proper interest of corporate issues in whose securities the insider trading takes place. If the person who takes the advantage of the information is a director or officer of the company or is in some clearly defined relationship involving confidence and trust within the company, the potential for harm is even greater. It is disadvantageous for a company to acquire a reputation of being an insider's company. Such a company may have problems in securing finance on competitive terms and the company suffers in the market as consequence of loss of respect in the integrity of its management.

Insider trading is the trading of a corporation's stock or other securities for example bonds or stock options by individuals with the potential access to non-public information about the company. However the term is frequently used to refer to a practice in which an insider or a related party trades based on material non-public information obtained during the performance of the insider's duties at the corporation or otherwise in breach of a fiduciary or other relationship of trust and confidence or where the non-public information was misappropriated from the company.[33]

In corporate law theory, insider trading refers to transactions in company's securities by corporate insiders or their associates based on information originating within the firm that

32 Ramirez, Gabriel G., Yung, Kenneth K, Tin, Jan, Firm Reputation and insider Trading: The Investment Banking Industry
33 Insider trading U.S Securities and Exchange Commission. Accessed May 7th 2008

would, once public disclosed, affect the prices of such securities.[34] The above definitions of insider trading make it inescapable not to talk about capital markets when discussing insider trading.

Globally, the evolution of capital markets in the last two decades has been dichotomous, in the sense that the markets have experienced integration as well as segmentation. On the one hand, some emerging capital markets have recorded a dramatic increase in foreign investment due to an expansion in privatisation listings, the use of bond instruments in international debt settlement and some successful implementation of economic stabilisation programmes. The inflows of foreign capital to the mature capital markets have enabled these markets to become more integrated with global markets. On the other hand, some very small, less developed capital markets, which are defined as 'frontier markets' by international Finance Corporation, have not received much of the foreign inflows. The markets have become consequently segmented from global markets. The dichotomous patterns of integration and segmentation have important consequences for the roles that these markets will play in emerging economies, particularly in Africa.[35]

The dichotomous evolution poses important challenges for the roles that these markets can play in emerging economies.[36] This research paper aims to examine the roles and challenges of capital markets, with special focus on Uganda.

Victor murinde defined Capital markets as markets for trading long term financial securities, including ordinary shares, long term debt securities such as debentures, unsecured loan stock and convertible bonds. Government bonds and other public sector securities such as treasury bills and gilt edged stocks are also traded on capital markets.

Capital markets play three main roles. First, long term funds can be raised by companies from those with funds to invest, such as financial institutions and private investors, in fulfilling this role, they act as primary markets for new issues of equity and debt. Second, capital markets provide a ready means for investors to sell shares and bonds they own, or to buy additional ones to increase their portfolios, in fulfilling this role, the capital markets act as secondary markets for trading existing securities. Third, the markets provide mechanisms for trading

34 Stanislav D, Insider Trading and the Bio-Ask Spread: A critical Evaluation of Adverse Selection in Market Making
35 Victor Murinde at page 1
36 Victor Murinde, Capital Markets: Roles and Challenges, University of Birmingham

future and contingent claims, based on the values of the underlying assets, hence the derivatives market.[37]

Justice Blackman made a bald assertion that insider dealing is inherently unfair,[38] a claim which quite highly lacks credibility in the eyes of deregulators and others since the concept of what is 'fair and what is 'unfair' are given no content.[39] As Easterbrook[40] says, 'without some further explanation... we cannot tell how fair fairness principles reach' However, this argument cannot on its own constitute the basis for regulation of insider trading as most deals are concluded at the stock exchange and those who deal with other persons.

The existing literature argues that insider traders can capitalise on their private information, with those receiving favourable information tending to buy the assets and those receiving unfavourable information tending to sell it. However very often, because of the ability of uninformed prices the insider may moderate his actions.[41]

While the debate will undoubtedly continue, the trend is not only to continue the prohibition but also to expand its coverage and increase the penalties for violation.

37 Ibid at 1
38 *US-V- Chiarella 445 US 222 p. 248-250*
39 Judith G. Greenberg, Insider Trading and Family Values, 4 WM & MARY J WOMEN & L. 303(1998)
40 United States-v-O'Hagan 97 C.D O.S 4931 at P. 323-3249 decided in June 25th, 1997
41 Meger Announcement and Insider Trading Activity. An Empirical Comparative Investigation in LSE and ASE at 2

CHAPTER TWO
CONCEPTUAL CLARIFICATION AND DEFINITION OF TERMS.

2.1 AN INSIDER

Over the years, there has been much controversy over the issue of who becomes an insider, where, how and when. For example some insiders did not gain their advantage through a specific discussion with insiders, but gathered the information either inadvertently or in an unguarded social setting.[42]

An insider is a person who has inside information through;

(i) Being a director, employee or shareholder of an issuer of securities listed on a regulated market to which the information relates or

(ii) Having access to such information by virtue of employment, office or profession or where such person knows that the direct or indirect source of the information was a person contemplated above.[43]

For example, a company director, employee, adviser or even a journalist becomes an insider when he or she is made aware of a proposed transaction that could affect the price or value of a listed security.

The potential pool of persons who could become insiders is large and relates not only to directors, employees and advisers but could also include advertising and production companies employed to compile and produce confidential information such as newspaper advertisement announcing company results, cautionary announcements and other price-sensitive notices. Those people involved in defining interest rate policy are also insiders in relation to government debt instruments.

In Uganda, two main paths have been followed to the definition of an insider namely first, the view emphasizing that for one to be an insider they must be connected to the company-the person connected approach. Secondly, the information based approach where emphasis is on the possession of inside information regardless of whether a person is connected to the company or not.[44] Thus the Capital Markets Authority Act follows the person connected approach of insider trading legislations and precludes insider dealing by an insider of the body corporate with which he is connected[45] and prohibits insider dealing of a person connected with one company from dealing with the securities of another company, if by

42 Insider trading and other Market Abuses(Including the Effective Management of Price Sensitive Information at page 7
43 Insider trading and other Market Abuses(Including the Effective Management of Price Sensitive Information at page 7
44Jimmy Walabyeki, Insider Trading in Uganda: An Analysis of the Capital Markets Regulatory Framework at 4
45section 88(1)

reason of his connection with the first company he gets inside information of the company. It distinguishes between primary and secondary insiders or tipees.

All insiders are fiduciaries but not all fiduciaries are insiders. An insider must be knowingly connected with issuer of the securities traded or have been connected with the issuer within the previous six months.[46]

Under the Capital Markets Authority Act, a primary insider is defined as a person who within the past six months immediately preceding a specific deal has been connected with a body corporate and possesses inside information[47]and includes both companies and individuals. For individuals, a person is connected to the company if they are an officer of that company or a related company,[48] a substantial shareholder in that company or in a related company. Alternatively, an individual is connected to the company if they occupy a position that may reasonably be expected to give them access to inside information by virtue of any professional or business relationship existing between them or their employer, and that company is a related company or a company of which he or she is an officer.

On the other hand, a company is connected to another when any of its officers is connected to the other company.[49]

Tipees

In Uganda, a person is precluded from dealing in securities if he gets information from an insider and knows or ought reasonably to know that the insider is disclosing inside information, and the insider would not be allowed to deal in those securities.[50] Alternatively, it provides that although a person is not an 'insider they shall not deal in the securities if they are associated with the insider or they had an arrangement with the insider to receive insider so that they can deal in securities on the basis of that information. This provision ensures that insiders do not circumvent the law, and seek to profit from inside information by leaking this information to a person who has no connection with the company whose securities are being traded. However, this provision puts an unduly heavy burden on the Director of Public Prosecution, to prove that there has been an arrangement or some formal association with the insider.

46 Barbara Ann Banoff, The Regulation of Insider Trading in the United States, United Kingdom and Japan at 155
47 Section 88(1)
48 Section 88(8)
49 Section 88(5)
50 Section 88

The Securities exchange limited insider Trading Rules 2008 also define who an insider is. Under the rules, the following are insiders;

(a) An insider is a person who is a board member, member of senior management, an employee in the finance department or any senior manager who by virtue of their duties would likely gain access to unpublished price sensitive information. A senior manager is an employee who is part of the top management of the organisation
(b) Has access to unpublished price sensitive information by virtue of his employment office or profession, or
(c) Is an immediate family member of the persons mentioned in (a) and
(d) Has access to unpublished price sensitive information from any of the persons mentioned in (a) or (b) above
(e) All corporations, partnerships, trusts or other entities owned or controlled by any of the above persons.

2.2 INSIDER INFORMATION

Inside information is "... specific or precise information, which has not been made public and which is obtained or learned as an insider and if it were made public, would be likely to have a material effect on the price or value of any security listed on a regulated market."[51]

Inside information is the information that it not generally available, but if it were, might materially affect the price of the securities of the company.[52] Thus not all information is deemed to be inside information although it may be unpublished information.[53] Prior to the 2016 amendment of Capital Markets Authority Act, the term information 'generally available' was not defined thus there was risk for one being liable for insider trading for trading on the basis of mere rumours or speculations implying that as they perform their duties, securities analysts and certain classes of journalists may be at risk.[54] In 2016, the Capital Markets (Amendment) Act defined information generally available to mean "information that has been known to persons who invest in securities of a kind, which is likely to affect the price or value and since the information was made known, a reasonable

51 Insider Trading and Other Market Abuses (Including the Effective Management of Price Sensitive Information at 5)

52 Capital Markets Authority Act, Cap. 84, section 88(1)
53 Hui Hang, The Regulation of Insider Trading in China: A critical Review and Proposals for Reform' (2005) 17, Australian Journal of Corporate Law at 9
54 O'Brien. Dara: Problems Facing Irish Insider Dealing Legislation and Proposals for An Alternative Approach' 2006-07, 3 Galway Student Review at 138

period for the information to be disseminated among, and assimilated by, such persons, has elapsed."[55]

Information in relation to securities include matters of supposition and other matters that are insufficiently definite to warrant their being made known to the public, matters relating to intentions or likely intentions of a person, matters relating to negotiations or proposals with respect to the activities of a relevant entity, or to dealing in securities. It also entails information relating to the financial performance of any relevant entity, information that a person proposes to enter into or has previously entered into, one or, more transaction arrangements or agreements in relation to securities or has prepared or proposes to issue a statement relating to such securities; and matters relating to the future.

The information must be price sensitive. Information is deemed to be price sensitive if there is a reasonable likelihood that it would be considered important to an investor in making a decision regarding the purchase or sale of securities. Price sensitive information is deemed to be non-public when it is not available to the general public. While it is not possible to define all categories of material information, there are various categories of information that are particularly sensitive and, as a general rule, should always be considered material.[56] Examples of such information include, financial results, projections of future earnings or losses of an exceptional nature, news of a pending or proposed merger, acquisitions or divestitures, impending bankruptcy or financial liquidity problems, new equity or debt offerings. It also includes significant litigation exposure due to actual or threatened litigation, major changes in directors and senior management, rights issues and corporate actions that are likely to affect investment decisions.

The information must materially affect the price or value of securities. This means the information that would tend, on becoming generally available, to influence reasonable persons who invest in securities in deciding whether or not to acquire or dispose of or retain such securities or enter into an agreement with a view to acquire or dispose of or retain those securities.[57]

According to the Association of Investment Management and Research (AIMR) Standards of Practice Handbook, inside information is generally defined as information of a company that is both material and non-public. Under the Securities Laws of United States, Information is

55 Section 59 of Capital Markets Authority (Amendment) Act 2016
56 Uganda Securities Exchange Limited Insider Trading Rules 2008, Rule 3
57 Section 88(11) as amended by section 59 of Capital Markets Authority(Amendment) Act 2016

material if a reasonable investor is likely to consider it significant in making an investment decision or if the information is reasonably certain to have a substantial impact on the market price of a company's securities.'[58]

Apart from financial data, inside information could include, for example, changes in the executive of the company through appointments or resignations, or even incapacity of a senior director through, for example, serious long-term illness. It may also include the acquisition or loss of major contracts, labour disputes or strikes, law suits, defaults and liquidations, competition commission investigations or rulings, qualified audits and product malfunctions.[59]

However, the legislation regulating insider trading in Uganda does not define non-public information nor does it explain when information becomes public.

Positive and Negative Information

The standard justification for regulating insider trading ignore the fact that there are two distinct types of insider trading: insider trading based upon positive information and insider trading based upon negative information. Positive information also known as price increasing insider trading is non-whistle-blower information, while negative information also known as price decreasing information is essentially a whistle-blower's facts made known. This distinction is relevant for insider trading debate, but it has not received much attention in the literature. In other words most scholars assume, at least implicitly, that price decreasing insider trading and price increasing insider trading should be handled in an equivalent fashion either both should be regulated or neither should.[60]

Nonetheless, a few researchers have recognised the crucial distinction between trading on positive insider information and trading on negative insider information, and explored the attractiveness of an asymmetric insider trading regime one that continued to regulate price increasing insider trading in the conventional manner, yet offered no or less stringent regulation of price increasing information.

Lambert offered a particularly lucid explanation of the asymmetric approach to insider trading regulation. He argued that affording different legal treatment to the two types of trading was justified by the fact that price decreasing insider trading provides significantly

58Insider Trading and Other Market Abuses (Including the Effective Management of Price Sensitive Information at 5)
59Insider Trading and Other Market Abuses (Including the Effective Management of Price Sensitive Information at 5)
60 Clark, Stephen Rhett. "Essays in insider trading, informational efficiency, and asset pricing." PhD (Doctor of Philosophy) thesis, University of Iowa, 2014 at page 17

more value to investors than did price increasing insider trading. The signalling effect of price decreasing trades would be amplified by requiring public announcement of these trades immediately upon execution, because executives would be less able to 'game' the system through strategic trading. Lambert argued that, under such a system-one where insiders could make price decreasing trades so long as they immediately announced the trades to the public-most negotiations would result in the adoption of asymmetric regimes. Hence he concluded that the regulators should establish such a policy as the default that would govern in the absence of express contracting.[61]

Grechenig verified the optimality of an asymmetric insider trading regime. Such a regime would deter corporate malfeasance because insider trading on negative information discloses concealed information to the market in a manner functionally equivalent to whistleblowing. Existing studies tend to indicate that important gains to the social welfare come with insider trading on negative information. Whereas losses frequently result from the use of positive information, these arguments prompted Grechenig to appeal to regulators to adopt an approach that would allow insiders to trade based on private price decreasing information.[62]

While this is a relatively new topic in the insider trading debate, existing literature tends to support an asymmetric approach to insider trading regulation. In particular, the studies indicate that social welfare would be enhanced if regulators allowed insiders to trade based on negative private information also known as price decreasing trades. Accordingly, the results in this section provides a measure of 'victory' for the anti-and self-regulation school of thought.

2.3.0 INSIDER DEALING

2.3.1 DEALING

The law regulating insider trading in Uganda defines a dealer and dealing in securities. Thus a dealer is a person who carries on a business of dealing in securities on his own account, whether he carries on any other business or not, but does not include an exempt dealer.[63]

Dealing in securities is said to arise where, a person acting as a principal or agent, makes or offers to make with any person, or induces or attempts to induce any person to enter into any agreement for or with a view of acquiring, disposing of, subscribing for or underwriting

61Lambert, T.A. (2006). Overvalued equity and the case for an asymmetric insider trading regime. Wake Forest Law Review, 41, 1045-1058

62Grechenig, K.R. (2008). Positive and negative information: Insider trading rethought. Insider Trading: Global Developments and Analysis, 245.

63 Section 1(n) of Capital Markets Authority Act Cap. 84

securities or any agreement whose purpose or intended purpose is to secure a profit to any of the parties from the yield of securities or by reference to fluctuations in the price of securities.[64]

The Uganda Securities Insider Trading Rules[65] categorise dealing, disclosing and encouraging as insider dealing. Thus it includes a person who deals in price affected securities as a result of non-public information that has come into his or her possession. Secondly, where one person encourages another person to deal in securities that are price affected securities in relation to the non-public information whether or not that other person knows.

Insider dealing also arises where the person dealing relies on a professional intermediary or is himself acting as a professional intermediary with regard to utilization of non-public information.

Lastly, insider dealing arises where a person discloses information otherwise than in the proper performance of the functions of his/her employment, office or profession to another person.

It is not necessary for a primary insider to know whether or not he had inside information when dealing in the securities for them to be caught by the provisions of the law. Thus one need not know that he was in possession of inside information when he dealt in the company's

Securities and the person need not have relied on that information for him to be caught by the law. The rationale for this position was stated by the United States Court of Appeal that "...there are the insiders, who almost by definition have a degree of knowledge that makes them culpable if they trade on inside information. As officers, directors or employees of a company, they are presumed to know when information is undisclosed. Because of their positions, insiders know when they have the kindof knowledge that is likely to affect the value of the stock."[66] However it has been argued perhaps reasonably that this standard is too wide and may result in prohibiting actions which are not themselves fraudulent. For fraud cases, there ought to be intent. There ought to be scienter in the offence of insider trading. Since criminal law exists to punish the culpable, and culpability is tied to the defendant's

64 Capital Markets Authority Act Cap. 84, section 1(0)
65 Rule 4
66 United States Securities Exchange-v-Monarch Fund 608 F. 2d 938

mensrea, a defendant who did not act culpably should not be criminally sanctioned.[67] Uganda is not alone in this regard as in France the courts have penalised any insider who dealt while in possession of inside information regardless of whether or not the insider relied on that information. It may also result in the imposition of sanctions against a person who is unaware of the criminal nature of his behaviour.[68] This approach should be maintained because to require proof of mensrea would further make it very difficult to secure a conviction thereby failing to achieve the purpose of the law. The strict standard ought to be maintained as it compels persons who are connected to the company to be careful about how they handle the company's inside information.[69]

2.3.2 ENCOURAGING

The insider who is precluded from dealing in securities is also precluded from encouraging a person to trade using the inside information. Thus a person is not allowed to cause, or procure any other person to deal in those securities.[70] In prohibiting encouraging, the law is geared towards preventing a body corporate's representative from being overzealous when making presentations to meetings of large shareholders or analysts.[71]

It should be noted that this prohibition does not extend to an insider who discourages another person from dealing in the company's securities and the researcher proposes that the provision be made to include a prohibition of disclosure of information for purposes of causing a person to refrain from trading. The British Institute of international Comparative Law, Comparative implementation of EU Directives (1) - Insider Dealing and Market Abuse' cited section 123(1) of the Financial Services and Markets Act, 2000 goes somewhat further and covers the situation where an insider encourages a third party to deal, by taking or refraining from taking any action.

2.3.3. DISCLOSURE

The Act also prohibits communication of the information to any person if trading in those securities is permitted on a stock exchange within or outside Uganda, and he knows or ought to reasonably know that the other person will make use of the information for the purposes of dealing or causing or procuring another person to deal in those securities.[72] While the

67 Kelly Strader, "Re Conceptualizing Insider Trading: United States-v-Newman and the Intent to Defraud Volume 80 Issue 4 Brooklyn Law Review at 1425
68 International Organisation of Securities Commission(IOSCO), Insider Trading: How Jurisdictions Regulate it: report of the Emerging Markets Committee of the International Organisation of Securities Commissions' (March 2003) at 12
69 Jimmy Walabyeki, Insider Trading in Uganda: An Analysis of the Capital Markets Regulatory Framework at 13
70 Section 88(4)
71 Richard Jooste, 'The Regulation of Insider Trading in South Africa-Another Attempt' 117 SALJ 2000 P. 284 at 295
72 Section 88(4) (b)

provision concerning dealing precludes dealing in securities traded in Uganda, the provision relating to encouraging refers to securities on stock market within and outside Uganda and it is not clear why it is so.

2.4 CAPITAL MARKETS

Capital markets are markets for trading long term financial securities, including ordinary shares, long term debt securities such as debentures, unsecured loan stock and convertible bonds. Government bonds and other public sector securities such as Treasury bills and gilt-edged stocks are also traded on capital markets.[73]

The legislation regulating capital markets in Uganda defines capital markets to mean a market where funds are raised from individual and institutional investors by companies and governments through sale of shares or issue of debt to fund the activities of the companies or governments.[74]

HISTORY OF INSIDER TRADING

This part gives a background of insider trading laws and their progression through history in the United States as well as in the United Kingdom. The United States has a longer history of large prosecutions for insider trading than the United Kingdom.[75]

The United States has a long history of seeing insider trading as "wrong" and "unfair"; therefore, it has "frowned upon" and regulated insider trading for almost as long as traded securities have been in existence.[76]

The United States was one of the first countries to address insider trading as a real problem in regard to the integrity of the country's financial markets.[77]

The United States golden era for successful prosecution of insider trading was in the 1980s with one of the most famous cases involving a Wall Street Journal reporter found guilty of 'mail and wire fraud.[78] Mr R. Foster Winnans was trading on names about to appear in his 'heard on the street' column and went to jail for 18 months for his actions. Shortly prior to this case, the Court convicted Ivan Boesky to three and a half years and fined him $ 100 million for insider trading. However, the case that has received the most

73 Victor Murinde supra at 1
74 Section 1, Capital Markets Authority Act Cap 84 as amended by Capital Markets Authority(Amendment) Act 2016
75 A brief History of Insider Trading, Mindful Money(available at http://www.mindful money.co.Uk/7650/economic Impact/a-brief-history-of insider trading.html.(comparing the history of UK and U.S. Insider trading laws and enforcement
76 Timeline: A Selected Wall Street Chronology, PBS IPTV, http://www.pbs.org/wgbh/americanexperience/features/timeline/crash/1/ (last visited Oct. 2, 2012)
77 Timeline: A Selected Wall Street Chronology. PBS. IPTV, http://www.pbs.org/wgbh/american experience/feature/timeline/crash/./ (last visited oct.2 2012
78 Ibid

attention in the United States was Martha Stewart in 2004, who sold $ 228000 in shares of biomedical fir, the day before the shares value plunged 15%, causing her to go to prison for six months.[79]

The United Kingdom, on the other hand, has a less impressive track record. Yet it has also had some large insider dealing cases, with the highest profile, involving Guiness taking over its rival drink firm Distillers. In the early 1990s, this case saw Guiness President Ernest Saunders jailed for two years.[80]

The beginning of the insider trading problem

The first example of insider trading in the United States occurred in very early in the country's history. In 1790, the U.S Federal government issued $ 80 million in bonds, refinancing all federal and States Revolutionary War debt.[81]This refinancing was the first major issue of publicity traded securities and the birth of the United States investment Markets.Then U.S Department of the Treasury Assistant Secretary William Duer appointed in 1789 attempted to capitalise on his government connections and his own position to make bets on the country's new debt.[82]Duer borrowed too heavily and overreached himself. In early 1792, he drove up securities prices to new highs. Then later in the year, the market crashed and panic resulted when Duer could not repay the large amounts of money he had borrowed to implement his plans. Duer's investment eventually soured in 1792 when the market bubble burst, causing bankruptcy and the first crash of Wall Street.[83]The New York City economy fell along with him and Duer died in debtor's prison shortly thereafter. **(JAMES SUPRA)**

Answer to the 1792 Market crash

After the crash of 1792, a number of brokers who were aware of Duer's actions that caused the panic and crash decided that self-regulation of the market was the answer to cleaning up trade practices.[84] Therefore, 24 brokers gathered on May 17, 1792, to sign the Buttonwood Agreement, which stipulated that the assembled brokers would only trade with other mutually recognised brokers. In 1817, the Buttonwood Group became

79 Kylie Franklin, 'U.S. V. UK. Insider Trading Laws: Who is the Top Dog?'
80 Ibid at 6
81Ibid at p 8-9
82 Randy James, Insider Trading; TIME MAG., NOV. 9, 2009, http://www.time.com /time/magazine/article/o, 9171, 1938727, 0. Html#ix22283tohoig
83 Randy James, Insider Trading; TIME MAG., NOV. 9, 2009, http://www.time.com /time/magazine/article/o, 9171, 1938727, 0. Html#ix22283tohoig
84 Scot B. Macdonald & Jane Elizabeth Hughes, 'Separating Fools from their Money: A History of American Financial Scandals at 32-33

the New York Stock & Exchange Board, which then became the New York Stock Exchange in 1863. Thus the Buttonwood Agreement began the United States' long history of self-regulation in the Securities Markets.

The Court's response to insider trading problem

After many more scandals involving insider-trading issues surfaced over the next 100 years and with no public regulation implemented during this time, the U.S. Supreme Court finally ruled on the issue.[85] Prior to this Supreme Court case, there was no rule of law making insider trading illegal.[86] In ***Strong v. Repide***[87] decided in 1909, the Court held that "[a] director upon whose action the value of the shares depends cannot avail of his knowledge of what his own action will be to acquire shares from those whom he intentionally keeps in ignorance of his expected action and the resulting value of the shares."

United Kingdom insider dealing

The United Kingdom's insider dealing regulations have nowhere near as extensive a history as the United States insider trading regulation.[88]

The United Kingdom is one of the leading financial centres of the world.[89]

In the United Kingdom, in contrast to the United States' attitude, up until the end of World War 2, the buying and selling of stocks in a company based on inside information was legitimate and wide spread.[90]

Then between the end of World War 2 and the late 1950s, the public began to perceive trading on inside information as unethical due to seeming unfairness of making personal private profits at the expense of shareholders. However, in the 1960s and 1970s the practice became prevalent again, in fact, in 1973, the Financial Editor of the Sunday Times described insider trading as the 'crime of being something in the city'.

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85 An example of a large scandal that occurred was government officials profiting from manipulating railroad stocks. CHARLES R. GEIST, WALL STREET: A HISTORY: FROM ITS BEGINNINGS TO THE FALL OF ENRON 30 (2004)

86 LAWRENCE M. SALINGER, ENCYCLOPEDIA OF WHITE-COLLAR & CORPORATE CRIME 429 (2004) (discussing the implications of Repide).

87 213 U.S. 419, 420 (1909)(setting forth the first law against insider trading).

88 Kylie Franklin, 'U.S. V. UK. Insider Trading Laws: Who is the Top Dog?' at 24

89 James Quinn, Britain Overtakes US as Top Financial Centre, The Telegraph October 8 2009

90 Margaret Cole, Director of Enforcement, FSA London School of Economics (March 17 2007). Available at http://www.fsagovuk /library/communication/speech)2007/0317-mc shtml) giving a background of insider dealing law in the United kingdom

CHAPTER THREE
THE LEGAL FRAMEWORK OF INSIDER TRADING IN UGANDAN CAPITAL MARKETS

3.0 Introduction

Until 1996, there was no law against insider trading in Uganda and there was no duty to disclose or abstain inside information. As in other areas, the law of insider trading is in a process of evolution. The first legislation[91] prohibiting insider trading was enacted in 1996 and it was substantially amended in 2016. Thus before 1996, insider trading was not illegal in Uganda. Subsequently, the following legislations prohibiting insider trading have been enacted by the Ugandan parliament.

3.1The Capital Markets Authority Act Cap 84

This legislation commenced on the 24th day of May, 1996. According to its preamble, it was an Act to establish a Capital Markets Authority for the purpose of promoting and facilitating the development of an orderly, fair and efficient capital markets industry in Uganda; to make provision with respect to stock exchanges, stockbrokers and other persons dealing in securities; and for certain offences relating to trading in securities; and for purposes connected with the foregoing.

Section 86 of the above legislation criminalises acts of circulating or disseminating any statements to the effect that the price of any securities of a body corporate will or is likely to rise or fall or be maintained by reason of any transaction entered into or other act or thing done in relation to the securities of that body corporate in contravention of any of the provisions of the act. Further as seen and as will still be discussed by the researcher, Section 88 of the act has defined insider trading and inside information.

3.2 The Capital Markets Authority(Amendment) Act 2011

This Act was assented to on the 24th day of June and commenced on the 8th of July 2011. This was an Act to amend the Capital Markets Authority Act to provide for the conversion of amounts in shillings into currency points; to provide for the offering of securities to the public; to empower the Authority to collect fines; for connected purposes.

Under this amendment, insider trading is not expressly forbidden and the researcher therefore draws prohibition of the same impliedly. Section 9 provides for a prospectus

91 The Capital Markets Authority Act Cap. 84

whose intendment is to advertise securities an issuer has to the public. Section 90k(1) provides that where a prospectus is required for an offer of securities, a person shall not advertise to the intended offerees or publish a statement that directly or indirectly refers to the offer or intended offer or is likely to induce persons to subscribe for or to purchase securities. The act has further prescribed penalties[92] for persons who contravene section 90K(1) above and such a person is on conviction penalized with a fine not exceeding two hundred currency points.

3.3 The capital Markets Authority (Amendment) Act 2016

This Act was assented to on the 3rd day of May 2016 and commenced on the 20th day of May 2016.

This was an Act to amend the Capital Markets Authority Act Cap 84; to provide for the establishment of the Board, its functions, meetings and committees of the Board of directors, the appointment of the Board secretary; the composition and functions of the Authority; power to require production of books by approved persons and key persons; power to search premises; assistance to foreign regulatory Authorities; duty to report; statement of principles and codes of practice; guidelines and regulatory notices; publication of information; public statements; exercise of disciplinary powers by the Authority; power to close or suspend trading; promotion and floatation of securities; grounds for approval of licenses; appointment of a statutory manager; appeals; establishment, constitution, functions and proceedings of the Capital Markets Tribunal; market abuse and for connected purposes.

This act clarifies who an insider is and further broadens the meaning the meaning of information in as far as insider trading is concerned.[93] Information that would materially affect the price or value of securities is information that would tend, on becoming generally available, influence reasonable persons who invest in securities in deciding whether or not to acquire or dispose of or retain such securities or enter into an agreement with a view to acquire or dispose of or retain such securities. The act under section 90AF has established a Capital Markets Tribunal whose functions inter alia is to deal with references referred to it by the Authority concerning inquiries into the conduct of a

92Section 90k(5), Capital Markets Authority (Amendment) Act, 2011.
93Section 59 Capital Markets Authority (Amendment) Act, 2016

licensed person or approved securities exchange or issuer or other market participant in relation to any conduct or activity affecting the securities market.

3.4 Capital Markets (Asset Backed Securities) Regulations, 2012 statutory instruments 2012 No. 46.

These Regulations were promulgated on the 29th of June 2012. The regulations were made by the Capital Markets Authority on the 7th day May 2017 while exercising its powers conferred upon it by section 101 of the Capital Markets Authority Act.

The Regulations applies to all offers of asset backed securities to the public or a section of this public in Uganda including issues by state corporations and other public bodies. The Regulations also applies to the Rules and Regulations governing the issue, offer and listing of fixed income securities shall apply to asset backed securities to the extent that they do not conflict with these Regulations.

To protect inside information, the regulations provide for an issuer to have an auditor under Regulation 12 who must be a member of the Institute of certified Public Accountants and whose place of business is Uganda. The regulations also prohibit the issuer from having an auditor who is an affiliate of any participant in the securitization transaction or a close relative of an officer or director of any participant in the securitisation.[94]

3.5The Capital Markets (Cross Border Introductions) Regulations, 2004(2004 No. 43)

These Regulations were also made by the Capital Markets Authority by virtue of its power given to it under section 101 of the Capital Markets Authority Act, Cap. 84.

Applicants for cross border introductions have to fill information memorandum containing information out lined in the 2nd schedule of the regulations. The regulations in the second schedule paragraph (f) and (g) provide that the information memorandum should not constitute an offer or invitation to any person to subscribe for or purchase any new shares in the applicant and the information memorandum should not market any new shares held by the applicant. The intendment of the above is not to let inside information of the applicant from being let to the public.

94Regulation 12(2b) Capital Markets (Asset Backed securities) regulations 2012, SI No 43/2012

3.6 Uganda Securities Exchange Limited Insider Trading Rules 2008

The Rules were made pursuant to section 24 of the Capital Markets Authority Act, Cap 84 and regulation 14 of the Capital Markets Authority(Establishment of Stock Exchanges) Regulations, Statutory Instrument 84-3)

Mindful of the fact that the secondary market in transferable securities plays an important role in the financing of economic agents. For the market to be able to play its role effectively, every measure should be taken to ensure that the market operates smoothly, the market should be seen to operate fairly and on the basis of equal information. The purpose of these rules is therefore to:

a) Boost investor confidence by creating conditions that ensure that fairness and equality of access to information exists in the market. The factors on which such confidence depends include the assurance afforded to investors that they are placed on an equal footing.

b) Reassure investors that they will be protected against the improper use of insider information. By benefiting certain investors as compared with others, insider dealing is likely to undermine the confidence and may therefore prejudice the smooth operation of the market.

c) To promote market efficiency, fairness and orderliness by ensuring that market participants privy to price sensitive information do not make use of it to the detriment of other investors before it is published.

The Uganda securities exchange,

Rule 2 of the rule defines an insider as defined in section 2 and further describes price sensitive information in section 3 as information to deem to be price sensitive if there is a reasonable likelihoodthat it would be considered important to an investor in making a decision regarding the purchase or sale of securities. The rules make price sensitive information non-public when not available to the general public. Examples of sensitive as under the rules are:

a. Financial results, projections of future earnings or losses of an exceptional nature, now of appending or proposed merger ,acquisitions/divesitives, impending bankruptcy or financial liquidity problems ,new equity or debt offerings, significant litigation exposure due to actual or threatened litigation, major exchanges in directors

and senior management, right issues, corporate actions that are likely to affect investment decisions.

The Rules under Rule 4 also provide for dealings that are deemed insider trading inter alia, any person dealing in price affected securities as a result of non-public information that has come into his or her position.

b. Encouraging another person to deal in securities that are whether or not that person knows price affected securities in relation the non-public information.
c. The person dealing relies on aprofessional intermediary or is himself acting as a professional intermediary with regard to utilisation of non-public information.
d. Any person disclosing information otherwise than the proper performance of the functions of his or her employment, office or profession to another person.

The rules under rule 7 penalise any person who contravenes the rules. It is to the effect that on suspicion of any contravention of the rule d by an insider,the exchange shall carryout an investigation and dependency on the outcome inter alia does the following:

- Step any trade by an insider if settlement of the trade has not yet been affected.
- Commence disciplinary proceedings against any person involved if such person is an employee of the exchange.
- Freeze the securities that are the subject of the investigation.

Further the rules provide that any person involved in the insider trader shall pay a penalty that shall be commensurate to the amount of money that he/she has made as a result of insider trading.

Establishment of the Capital Markets Authority

The Capital Markets Authority Act[95] establishes the Authority whose objectives as set out by the Capital Markets Authority Amendment Act of 2016[96] are the following; to promote confidence in the capital markets, to ensure honesty and transparency in capital markets transactions, to carry out investor education, to protect investors and to reduce systemic risk.

The functions of the Authority are also stipulated by the Amendment Act of 2016 and they are;

95 Section 4(1)
96 Section 4B

(a) To approve prospectuses and other offering documents under which securities are offered to the public and to approve information memorandum;

(b) To develop all aspects of the capital markets with particular emphasis on the removal of impediments to, and the creation of incentives for, long term investments in productive enterprise;

(c) to create, maintain and regulate, through implementation of a system in which the market participants are self-regulatory to the maximum practicable extent, of a market in which securities can be issued and traded in an orderly, fair and efficient manner;

(d) To cooperate with, provide information to, conduct any investigation or inquiry for, or otherwise assist any foreign regulatory authority in the performance of its duties;

(e) To implement regional and international standards and best practice in securities markets, securities regulation and supervision;

(f) To protect investor interests; and

(g) To operate the Investor Compensation Fund

For the purpose of carrying out its objects, the Authority may advise the Minister on all matters relating to the development and operation of capital markets, maintain surveillance over securities to ensure orderly, fair and equitable dealings in securities, grant a licence to any person to operate as a stockbroker, dealer or investment adviser, fund manager, investment house, collective investment scheme, market adviser, representative, trustee, custodian or depository; and ensure the proper conduct of that business, grant approval to any person to operate as a commodities exchange, securities exchange, securities central depository, credit rating agency, registrar, underwriter, clearing house, clearance and settlement facility or to operate in any other capacity which directly contributes to the attainment of the objectives of this Act; and to ensure the proper conduct of that business, approve venture capital funds, approve any other persons dealing in securities or exercising any functions related to securities, and their agents and to control and supervise their activities with a view to maintaining proper standards of conduct and professionalism in the securities business, inquire into the affairs or conduct of any approved person and to hear and determine any complaints concerning any act or omission, which, if proven, would be a breach of this Act and to refer, in its discretion, that inquiry or complaint to the Capital Markets Tribunal, publish, when the Authority considers it appropriate, any report or

comment made by the Authority in the course of the exercise of its functions, conduct any investigation or inquiry relevant to the securities markets in Uganda or elsewhere and publish any report arising from that investigation or inquiry, make and maintain effective arrangements for consulting practitioners and consumers on its general policies and proposed legislative measures for the capital markets industry, formulate principles for the guidance of the securities industry, monitor the solvency of licence holders and take measures to protect the interests of customers where the solvency of any licence holder is in doubt, protect the integrity of the securities market against any abuses, monitor takeovers and mergers in respect of listed companies in Uganda and adopt measures for the supervision and regulation of takeovers and mergers in order to protect the interests of investors and to provide for an orderly and well-informed capital markets, formulate measures to minimise and supervise any conflict of interest that may arise for licensed persons and the Authority, create the necessary environment for the orderly growth and development of the capital markets, co-operate with and enter into agreements for mutual co-operation and assistance with other regulatory authorities, whether within or outside Uganda, for the development and regulation of cross border activities in capital markets and provide assistance and information to those authorities, perform the functions conferred on the Authority by the Companies Act, 2012, implement East African Community Council regulation directives, decisions or recommendations relating to the securities markets in the East African Region, trace and freeze any assets, including the bank accounts of any person who, upon investigation by the Authority, is found to have engaged in any fraudulent dealings in securities or insider trading, act as the supervisory authority for anti-money laundering and combating of financing of terrorism in the capital markets and perform the functions conferred on the Authority, as an accountable person, under the Anti-Money Laundering Act, 2013 and undertake such other activities as are necessary or expedient for giving full effect to the provisions of this Act.[97]

97 Section 5(2) of the Capital Markets Authority (Amendment) Act 2016

CHAPTER FOUR
ANALYSIS OF THE LEGAL FRAMEWORK OF INSIDER TRADING IN UGANDA CAPITAL MARKETS

4.0 introduction

As the preceding discussion indicates, no resolution has been reached regarding the desirability of insider trading regulations,[98] the researcher will now consider, regardless of whether the regulations are necessary, if enforcement actions brought under existing regulations are effective this will help the researcher answer research question number five. The existing regulations against insider trading categorically define inside trades and the features incidental their under, they go ahead to prescribe punishment for insider trading. For example the Uganda Securities Exchange Limited Insider Trading Rules 2008, prescribes penalties[99] for anyone who deals in insider trade. What however is lacking in the legal framework is how anyone who would engage in insider trade would be detected and who would actually effectuate the penalty handed down to him basing on the rules of natural justice. This chapter therefore gives a background of insider trading laws in Uganda, their progression through history and the development of regulations to prevent insider trading in Uganda. Uganda has a less impressive track record of insider trading. The researcher will then recommend effective methods of dealing with insider trading basing on the fact that the current regulations don't touch the root method of how to deal with insider trading but rather make scanty provisions against the same.

This study is on the insider trading framework of Uganda. The researcher has made enquiries whether the Uganda legal framework governing insider trading provides strong enough enforcement mechanisms, including remedies and measures against malpractices found on the securities market to attract investor confidence. Critical analysis is done of the Capital Markets and Authority Act, Cap 84 as amended in conjunction with an investigation into the Capital Markets Authority (CMA) a body corporate charged with the duties among others, of protecting the integrity of the securities market and maintaining surveillance over securities to ensure orderly, fair and equitable dealings in securities.

In this chapter, the researcher examines the Capital Market Authority Act in terms of fulfilling its roles, functions, and powers. It is submitted that the Capital Market Authority

98 Clark, Stephen Rhett. "Essays in insider trading, informational efficiency, and asset pricing." PhD (Doctor of Philosophy) thesis, University of Iowa, 2014 at page 26
99Rule 7, USE Insider trading rules.

Act and the Authority have never contributed much to resolving the problem of securities market abuses.

4.1 Prohibition of insider trading.

Under the Capital Markets Authority Act, a person who is or has at any time in the six months immediately preceding a specific deal, been connected with a body corporate shall not deal in any securities of that body corporate if by reason of his association he is in possession of information that is not generally available but, if it were, might materially affect the price of those securities.[100]

Also a person who is or has at any time in the preceding six months immediately preceding a specific deal, been connected with a body corporate shall not deal in any securities of another body corporate if by reason of his being, or having been, connected with the first-mentioned body corporate he is in possession of information is not generally available but, if it were, would be likely to affect materially the price of those securities and relates to any transaction whether actual or expected involving both those bodies corporate or involving one of them and the securities of the other.[101]

4.2 Understanding who an insider is.

An Insider is any person who, is or was connected with a company or is deemed to have been connected with a company, and who is reasonably expected to have access, by virtue of that connection, to unpublished information which, if made generally available, would be likely to materially affect the price or value of the securities of the company, or who has received or has had access to such unpublished information.[102]

As seen from above definition, two main paths have been followed as to the definition of an insider namely first, the view emphasizing that for one to be an insider they must be connected to the company- the person connected approach. Secondly, the information based approach where emphasis is on the possession of inside information regardless of whether a person is connected to the company or not. The insider trading legislation follows the person connected approach of insider trading legislation, and precludes insider dealing by an insider of the body corporate with which he is connected, and prohibits insider dealing of a person connected with one company from dealing with the securities of another company, if by reason of his connection with the first

100 Section 88(1), Cap 84
101 Section 88(2)
102 Capital Markets Authority Act Cap 84 as amended , Section 88(11)

company, he gets inside information of the other company. It distinguishes between primary insiders and secondary insiders or tipees. Under the law, a primary insider is a person who within the past six months immediately preceding a specific deal has been connected with a body corporate and possesses inside information[103]and includes both companies and individuals. For individuals, a person is connected to the company if they are an officer of that company or of a related company, a substantial shareholder in that company or in a related company.[104]Alternatively, an individual is connected to the company if they occupy a position that may reasonably be expected to give them access to inside information by virtue of any professional or business relationship existing between them or their employer, and that company or a related company or a company of which he or she is an officer.[105]

The Uganda Securities Exchange Limited Insider Trading Rules 2008and the Capital Markets Authority (Amendment) Act 2016, have widened the scope of a person to include juristic persons. The Act also defines an insider as any person who, is or was connected with a company or is deemed to have been connected with a company. This widening of the scope of a person to some extent makes the law comprehensive thus a commendable notion as it expands the scope of a person to include array of juristic persons.[106]The law also clearly defines an officer in relation to an issuer or other body corporate to include; a director, secretary, executive officer or employee of the issuer or other body corporate. A receiver, or receiver and manager, of property of the issuer or body corporate. A liquidator of the issuer or body corporate; and a trustee or other person administering a compromise or arrangement made between the issuer or body corporate and another person.

4.3 Clarification of the meaning of inside information.

The current legal framework has clarified on the meaning of inside information upon which one may be liable if he trades on the basis of such information. The Capital Markets authority Act(Amendment) Act, under section 59, information in relation to securities includes:- matters of supposition and other matters that are insufficiently definite to warrant their being made known to the public, matters relating to intentions or likely intentions of a person,

103 Capital Markets Authority Act, Section 88(1)
104 Capital Markets Authority Act, section 88(8)
105 Officer is defined in Section 88(11) of the Capital Markets Authority Act Chapter 84 as amended, to include '(a) a director, a secretary, an executive officer or an employee of the body corporate; (b) a receiver, or a receiver and manager, of property of the body corporate; (c) an official manager or a deputy official manager of the body corporate; (d) a liquidator of the body corporate; and (e) a trustee or other person administering a compromise or arrangement made between the body corporate and another person.
106 Rule 2

matters relating to negotiations or proposals with respect to the activities of a relevant entity, or to dealings in securities, information relating to the financial performance of any relevant entity and information that a person proposes to enter into, or has previously entered into, one or more transactions, arrangements or agreements in relation to securities or has prepared or proposes to issue a statement relating to such securities; and matters relating to the future.

The current legal framework also defines what it means for information generally available. Under section 59, 'information generally available' means information that has been made known to persons who invest in securities of a kind, which is likely to affect the price or value and since the information was made known, a reasonable period for the information to be disseminated among, and assimilated by, such persons, has elapsed. The reason for drawing the dichotomy between precise information and general information is because the degree of specificity of information affects the level of risk which an investor would be taking. The more specific the information is, the less risk the investor would face and the more general the information is the greater the risk the investor would be likely to bear.[107]

The legal framework also defines information that materially affect the price or value of securities. Under the current legal framework, 'materially affect the price or value of securities means information that would tend, on becoming generally available, to influence reasonable persons who invest in securities in deciding whether or not to acquire or dispose of or retain such securities or enter into an agreement with a view to acquire or dispose of or retain those securities. This has served to avoid any uncertainties that may arise as to determining the degree of materiality.[108]It is the researcher's view that this clarification of inside information has ensured that information be of a precise nature to ensure that persons who act on general information are not prosecuted.

4.4 Scope of legislation.

The law on insider trading commendably covers a broad range of securities including debentures, stock, or bonds issued or proposed to be issued by a government; debentures, stocks, shares, bonds or notes issued or proposed to be issued by a body corporate; or any right, warrant, option, or futures in respect of any debenture, stocks, shares, bonds, notes or in respect of commodities; or any instruments commonly known as securities.[109] The justification for the legislation to cover only listed companies excluding companies which

107 United States Securities Exchange-v- Monarch Fund 608 F.2d 938.
108 The Griffith's report on Insider Trading in Australia(1989) (at XV of the summary of the findings)
109 Section 1 (hh) of Cap 84

are not listed is justified because insider trading, does greater harm to small retail investors[110] of listed companies compared to those companies whose shares have not been listed. However, the scope of the Act does not cover a company's cross listed shares in a jurisdiction outside Uganda. Thus, shares of a company whose shares are listed on the Uganda Securities Exchange, would be covered by the Act, but its shares on the Nairobi Stock exchange, would fall outside the jurisdiction of the Act because the Act only covers companies' shares within the jurisdiction of Uganda. This means that an insider in Uganda could still deal in securities of his company on the Nairobi Stock Exchange and not be caught by the provisions of the Capital Markets Authority Act[111]. It is therefore proposed that the definition of securities include securities traded on any regulated stock market,[112] which would include cross listed shares within the different stock markets in East Africa.

4.5 Interest in securities

According to insider trading legislation,[113]any property held in trust and consisting of or including securities in which a person knows or has reasonable grounds for believing that he has an interest, shall be taken to have an interest in those activities. Where a body corporate has an interest in the security and the body corporate or its directors are under an obligation to act in accordance with the directions or wishes of a person that person shall be taken to have interest in that security.[114]

A person also has an interest if he/she has a controlling interest in the body corporate or if the person or associates of that person are entitled to exercise or control the exercise of not less than 15% of the votes attached to the voting shares in the body corporate.

This comprehensive definition of interest in securities is important because the Capital Markets Authority Act[115]as amended emphasizes that insider trading arises where insiders deal with securities in a manner that is contrary to its provisions.

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110 International organisation of Securities Commission (IOSCO), Insider Trading: How Jurisdictions Regulate It: Report of the Emerging Markets Committee of the International Organisation of Securities Commissions'. March 2003 P. 6
111Chapter 84
112 The British Institute of International and Comparative Law. 'Comparative Implementation of European Union Directives (1) –Insider Dealing and Market Abuse'(December 2005) P. 10
113 Capital Markets Authority Act, section 3(1)
114 Ibid, section 3(2)(a)
115 Cap 84

Criminal Liability.

Under the Insider Trading legislation,[116] a person who contravenes any of the provisions prohibiting insider trading if he is a person not being a body corporate is on conviction liable to a fine not exceeding 10 million shillings or imprisonment not exceeding 5 years or both. Where a person convicted is a body corporate, the entity is liable to pay a fine not exceeding 12 million shillings.[117] The burden of proof is the ordinary proof in criminal cases which is proof beyond reasonable doubt which makes it difficult to obtain a conviction because insider trading cases are very difficult to prove.

Civil liability

The compensation paid by a convicted person is paid to any person with whom a transaction for the purchase was entered into with who suffers loss because of the difference between the price at which the securities were dealt in and the price at which they might have been dealt in at the time when the transaction took place if the contravention had not occurred.[118]The amount of compensation which a person is liable to pay is the amount of the loss sustained by the person claiming the compensation.[119]

The researcher reasonably submits that civil sanctions are difficult to invoke successfully. The civil remedy can only be invoked if there has been a conviction first under criminal liability since the Act provides that a *person convicted of an offence* is liable to pay compensation. Commendably, the current legal framework imposes sanctions for both profit made and loss avoided.[120] The extension of liability to recover loss avoided has provided an additional deterrent effect to potential of insider trading.

Suits by the Authority.

Where a civil suit is brought by the authority upon proof that a person contravened any of the provisions prohibiting insider trading, the person is liable to pay to the Authority the amount which the person profited or the loss which he avoided as a result of the contravention.[121]The court is also given discretion to make punitive or compensatory penalty not exceeding three times the amount or profit gained or the amount of loss avoided as a result of the

116 Capital Markets Authority Act Cap 84, section 89(1)
117 Ibid, section 89 (1) (b)
118 Capital Markets Authority Act. Cap 84 section 89(2)
119 Capital Markets Authority Act, Cap 84 as amended in 2016, section 89(8)
120 Ibid section 89(9) (b)
121 section 89(9)Capital Markets Authority Act, Cap 84, as amended in 2016

contravention.[122] The court can also determine interest and costs to be paid by a person who has violated insider Trading legislation. It is the researchers' view that the provisions of insider trading are not an adequate deterrent to insider trading. These sanctions inadequate most especially where insider trading involve colossal sums of money.

Investigation and Inspection by the Authority

The Authority has powers to carry out investigations where it has reasonable grounds to believe among others that there has been a contravention of the provisions of this Act, that it may be necessary to prohibit trading in securities under section 88, that a person has contravened the provisions of the Companies Act in relation to the securities of a company that are publicly held, that a body corporate or any officer of that body corporate or any person may have contravened the provisions of this Act or any applicable listing rules and that an approved person or key person may not be a fit and proper person to continue to be an approved person or key person.[123]

Inspection

The authority also has powers to inspect or appoint a person to inspect the books, accounts documents and transactions of an approved person.[124] The approved is enjoined to afford the authority access to and produce its or his books, accounts and documents and give such information and facilities as may be required to conduct the inspection.[125]Any approved person who fails, without reasonable excuse, to produce any book, account or document or furnish any information or facilities commits an offence and is liable on conviction to a fine not exceeding four million shillings or imprisonment not exceeding two years or both.[126]

It is the researcher's view that investigations and inspection are important in order to maintain or enhance the integrity of the Ugandan capital markets.

Disclosure to Authority

In order to fulfil the provisions of insider trading legislation, where it considers it necessary, the Authority may require an approved person to disclose to it, in relation to any acquisition or disposal of securities, the name of the person from or through whom or on whose behalf the securities were acquired or disposed of and the nature of the instructions given to the

122 Ibid section 89(9)
123, Section 19 Capital Markets Authority Act Cap 84 as amended in 2016
124 Cap 84as amended in 2016, Section 20
125 Ibid Section 20(3)
126 Ibid, Section 20(5)

stock broker, dealer or fund manager in respect of the acquisition or disposal.[127]The person who has acquired, held or disposed of securities may be required to disclose whether he held or disposed of the securities as trustee for or on behalf of another person or as a nominee, whether there is any other person who is a beneficial owner of the securities, the name of any person on whose behalf he or she has acted or who is a beneficial owner of the securities and the nature of any instruction given to that person as trustee or nominee in respect of the acquisition, holding or disposal.

Any person who fails to disclose to the authority when required commits an offence and is liable, on conviction, to a fine not exceeding one hundred currency points or imprisonment not exceeding two years, or both.[128]

Establishment of stock market

A person shall not carry on the business of a securities exchange or a commodities exchange unless that person has been approved by the Authority as a securities exchange or commodities exchange.[129]

Licenses

Under the insider trading legal framework, no person is allowed to act as a stock broker, dealer, a commodities exchanger or a stock exchange unless that person is approved to carry out that activity under this Act.[130] Any person who acts as any of the above without a valid license commits an offence and is liable on conviction to a fine not exceeding three hundred currency points or imprisonment not exceeding three years, or both.[131]

The researcher can comfortably state that Uganda's markets supervision does not have sophisticated technology and procedures to assist in the early detection of potential breaches of our insider trading laws and other forms of market manipulation. There is lack of a dedicated specialist insider trading unit. Uganda also lacks securities market automated research trading and surveillance which is a computer system monitoring all real-time trading information and high lights any unusual price.

127 Ibid, section 17
128 Ibid, section 17(5)
129 Ibid section 23
130 Ibid, Section 30
131 Ibid section 30(6)

While studies of legislation in other jurisdictions indicate that enforcement actions effectively deter managers from engaging in illegal insider trading,[132] the support for the position that these actions are not effective is more ample.

132 Cox, C.C., & Fogarty, K.S. (1988). Bases of insider trading law. Ohio State. Law Journal, 49, 353

CHAPTER FIVE
CONCLUSION

5.0 Introduction

Across the world, the amount of asset intermediation through stock markets has exceeded the same through banks in the recent years. Despite global economic Meltdown in the recent times, it is expected that trend will continue in the years to come. In contradiction to our earlier belief of the American supremacy in the global financial market the world is experiencing multiple parallel economic superpowers in many continents across the world. As a result we will find more asset intermediation through stock market and thereby increasing its importance. With the pace of growth in volume and depth, resilience in the equity market all over the world is expected to grow. The factors that made it possible this shift from banking orientation towards stock market orientation are fair price discovery, enhanced liquidity and declining transaction cost In contradiction to these pro market conditions number of anti market practices viz., price rigging, lack of transparency and fraudulent financial accounting practices in the published company accounts, excessive speculation etc. are also accentuating at an alarming pace. But the single problem that sometime outweighs the magnitude of the other problems is insider trading. Along with the growth of the global equity market severity, intensity and magnitude of the problem of the insider trading is also expected to grow over time. Regulators, despite all inherent problems within themselves, will try to come up with more comprehensive and rule based regulations to combat this problems. On the other hand, individuals and institutions will be continuously evolving with finer, e-based and cross border techniques of insider trading that seeks to tackle the regulatory hurdles-national as well as international. As a result, despite having anti-insider trading regulations in most of the organised securities market, the regulators would continue with better and finer rule based regulations of insider trading on a continues basis.

Although insider trading is a global phenomenon, its intensity is much higher in underdeveloped securities market.

It is often claimed that insider trading reduces investors' confidence in the market. Behind huge foreign investment in the United States many critics find the presence as well as strict enforcement of insider trading laws. If confidence in the market really decreases when insider trading exits then deregulation of the financial market is the most effective way to increase investors' confidence. Stock exchanges that have private rules of forbidding insider trading will attract more insiders and companies wish to have their stock listed on these exchanges.

The free market can provide for sensible insider trading rules without government intervention.

This concluding chapter is divided into two sections. In section 5.1 summary is provided of the contents of different chapters including the key findings of the study. Section 5.2 is designed to offer the potential policy guidelines for combating the problem of insider trading in Uganda.

5.1 Summary of the investigation and findings.

After narration of the aim, scope and methodology an indication has been given along with usual details as to how the study would be undertaken in chapter-1. Chapter-2 has been devoted to investigation into the conceptual clarifications and definition of terms . This is an important chapter that brings out the background of insider trading laws and their progressions through history. The chapter defines an insider in the Ugandan perspective firstly as, the view emphasizing that for one to be an insider they must be connected to the company- the person connected approach. Secondly, the information based approach where emphasis is on the possession of inside information regardless of whether a person is connected to the company or not. Insider information is "... specific or precise information, which has not been made public and which is obtained or learned as an insider and if it were made public, would be likely to have a material effect on the price or value of any security listed on a regulated market." The chapter defines many other terms relating to the project for example Tipees, capital markets and provides various information on the different terms.

Chapter- 3 has examined the legal frame work of insider trading in Ugandan Capital Markets. Until 1996, insider trading was not against the law in Uganda and there was not duty to disclose or abstain inside information. In other jurisdictions, the law against insider trading is in a process of evolution. The first legislation prohibiting insider trading in Uganda was enacted in 1996 and it was substantially amended in 2016. There are a number of legislations that have been put in place to regulate Insider trade in Uganda and they include the Capital Market authority Act Cap 84 which commenced on 24th day of May 1996 which according to its preamble was an Act to establish a Capital Markets Authority for the purpose of promoting and facilitating the development of an orderly, fair and efficient capital markets industry in Uganda; to make provision with respect to stock exchanges, stockbrokers and other persons dealing in securities; and for certain offences relating to trading in securities; and for purposes connected with the foregoing. The Capital Markets Authority (Amendment) Act 2011 was an Act to amend the Capital Markets Authority Act to provide for the conversion of amounts in shillings into currency points; to provide for the offering of

securities to the public; to empower the Authority to collect fines; for connected purposes.The capital Markets Authority (Amendment) Act 2016 This was an Act to amend the Capital Markets Authority Act Cap 84; to provide for the establishment of the Board, its functions, meetings and committees of the Board of directors, the appointment of the Board secretary; the composition and functions of the Authority; power to require production of books by approved persons and key persons; power to search premises; assistance to foreign regulatory Authorities; duty to report; statement of principles and codes of practice; guidelines and regulatory notices; publication of information; public statements; exercise of disciplinary powers by the Authority; power to close or suspend trading; promotion and floatation of securities; grounds for approval of licenses; appointment of a statutory manager; appeals; establishment, constitution, functions and proceedings of the Capital Markets Tribunal; market abuse and for connected purposes. Capital Markets (Asset Backed Securities) Regulations, 2012 statutory instruments 2012 No. 46. The Regulations applies to all offers of asset backed securities to the public or a section of this public in Uganda including issues by state corporations and other public bodies. The Regulations also applies to the Rules and Regulations governing the issue, offer and listing of fixed income securities shall apply to asset backed securities to the extent that they do not conflict with these Regulations. The Capital Markets (Cross Border Introductions) Regulations, 2004(2004 No. 43) Applicants for cross border introductions have to fill information memorandum containing information out lined in the 2nd schedule of the regulations. The regulations in the second schedule paragraph (f) and (g) provide that the information memorandum should not constitute an offer or invitation to any person to subscribe for or purchase any new shares in the applicant and the information memorandum should not market any new shares held by the applicant. The intendment of the above is not to let inside information of the applicant from being let to the public. Uganda Securities Exchange Limited Insider Trading Rules 2008The Rules were made pursuant to section 24 of the Capital Markets Authority Act, Cap 84 and regulation 14 of the Capital Markets Authority (Establishment of Stock Exchanges) Regulations, Statutory Instrument 84-3)

Chapter 4 establishes the analysis on the legal framework of insider trading in the Ugandan capital market and then chapter 5 analyses the conclusion and establishes the summary of findings and the recommendations borrowing a leaf from more developed economies.

5.2 Recommendations

Insider trading is a most controversial area of research and far more difficult is either to draw any general conclusions or to suggest any specific policy implication which would be a full proof one. During the last few years many well known companies both national as well as international have been found to be associated with this crime. SEC and other prominent regulatory bodies have suggested exhaustive list of measures, which are suggested to be adopted by the securities markets across the globe. In number of cases- Ugandan as well foreign, it has been noticed that anomalies remains not only in loosely drafted regulation but also in their ineffective implementations. Self-Regulatory Organisations (SROs) can take a predominant role in implementing insider trading regulations mainly defining disclosure requirements, defining procedures for handling inside information, defining restrictions concerning trading by insiders, limiting possibilities of trading based on inside information and investors education. In view of the above, following policy implications are considered to be useful.

5.2.1 Strengthening anti-insider drives and introducing insider trading task force

Capital Markets Authority has already made it compulsory that any significant contract for Purchase and sale of securities above a specified percentage of the total number of shares of the company must be published by the stock exchange. Failure to make such disclosure attracts penal action. At present the Capital Markets Authority has the right to initiate criminal prosecution against an insider for violation of insider trading regulations .Such prosecution may lead to imprisonment for a term which may extend to five year with fine or with both. In the USA, civil as well as criminal penal actions are allowed to be taken against insider trading offences. Penal measures are more rigorous which could lead to ten years of rigorous imprisonment and or cash penalty that too may lead to a maximum sum of 1 million dollars for individuals and 2.5 million dollars for companies. Considering the gravity of the situation I suggest that disclosures should be made obligatory at a lower percentage of holding at all levels and penal measures should be more rigid. With the spread of Ugandan stock market trading operations among the different foreign countries it is assumed that the nature of this problem will be more complex in the coming days.

SEC has already gained a commendable experience in this regard. In their anti-insider trading drive, SEC is currently exploring even the foreign countries where the insider trading takes place in relation to securities listed in their exchanges. If permitted, this anti-insider trading squad of Capital Markets Authority should be sent to SEC or other advanced

securities market regulators for their training. In USA there exists a very good provision in SEC regulation. Anyone who supplies information to SEC are amply rewarded. It helps insider trading investigation squad to probe into this complex issue and to obtain circumstantial evidence to book the culprit. The amounts recovered by the SEC or Attorney General from imposition of penalty for insider trading, not exceeding 10% of such amounts as the commission deems appropriate, paid to the person or persons who provide information leading to the imposition of such penalty. In Uganda such provisions should be introduce so that information about insiders may be easily available to the regulators or investigating officers.

There exists Insider Trading Task Force in Canada. Squads of similar nature, exclusively on insider trading investigation exists in USA. Those Squads are competent for inter-country investigation and may take independent legal action against the victims. No such exclusive force has ever been established in Uganda. Formation of such force with legal back up is strongly suggested in Uganda.

5.2.2 Application of circuit breakers mechanism on the basis of empirical research

Transactions in the Ugandan stock exchanges can be stopped or suspended in four different ways. Buy fridge, sell fridge, circuit filters and the closure of the whole exchange. However, transactions unofficially may continue in grey market. These closures of transactions are generally taken by the exchange authorities when it is perceived that a completely artificially arranged price gives benefit to a select few and neglects the interest of the mass. Some of such instances are cornering, wash sale etc.

Cornering is the practice of buying or holding of the entire supply of a particular security. In such a situation the bears or short sellers who have contracted to sell the security without possessing the same would be unable to deliver it to the buyers who have cornered the security. The buyers in this situation may dictate terms to the short sellers. In this way, the short sellers are squeezed to adopt the commonly adopted practice, which also goes against the interest of the common investors. On the other hand, when a speculator enters a fictitious transaction in which he sells a particular security through one broker and buys the same at a higher price through another broker the transaction is a wash sale transaction. It creates a false and misleading opinion about the price of the stock market when the price picks up speculators simply wash-off their hands by selling their scrip's. Sometimes, the speculators give orders to different brokers for the sale and purchase of a particular security i.e. orders are matched. This creates an impression in their market that the security is being actively traded and the price starts rising upward. The speculators off-load their holding when they consider

that the price has attained its peak. Once again, it is only the helpless common investors who suffer.

When authorities feel that majority of the common investors are buying scrip without taking note of the fundamentals or there is nexus between unscrupulous brokers to hike up the price artificially, they adopt buy fridge technique when common investors are not allowed to buy for a certain period of time. In a reverse situation there might be a situation to bring down the price artificially and investors may sell out of panic. In that situation the strategy on the part of the exchanges could be sell fridge. On the other hand when exchange authority feels a high degree of speculation but cannot determine the direction, they might go for circuit filters i.e., they determine the price range within which price may be allowed to oscillate. Circuit breaker is a different method. If price of scrip opens next day with a difference of 16% or more in comparison to its previous day, transaction in that scrip may be stopped for a few days.

Due to these types of artificial activities, when market volatility goes to an extreme level measures like buy fridge, sell fridge, circuit filters, circuit breakers or market closure methodologies are adopted. No empirical research is being conducted by the Exchanges in Uganda to adopt such policies. In developed stock exchanges like NASDAQ, New York Stock Exchange (NYSE) or American Stock Exchange (AMEX) the same is based on empirical research. I suggest our stock exchange to go for empirical research and adopt internal regulation to monitor our trading procedures on the basis of empirical research in line with NYSE or AMEX.

5.2.3 Ensuring better financial disclosure and harmonization of disclosure requirements

It is widely recognised fact that the stock market needs a steady flow of reliable of high quality corporate financial information to assess investment risks and returns. Corporate-credibility is the foundation on which investors base their confidence in the future success of the enterprise. This confidence may be damaged if it is revealed that an enterprise has followed less than rigorous standards in generating information provided to the shareholders. Full and fair disclosure of financial information in the financial statements has the effect of lowering the cost of capital. First path to lower cost of equity capital involves reducing the so called information risk that confronts all investors. If the available information is not adequate, investors are more uncertain about their estimates, which inject an additional element of risk into their assessment of the value of the firm. The second path to lower cost of capital is through a greater liquidity in the market for the firm's securities. Enhanced

public disclosure reduces information asymmetry among investors and as a result market liquidity for securities increases. Greater liquidity enhances demand for the firm's security and lowers cost of capital.

Ugandan companies have to make disclosures under the Capital Markets Authority(amendment) Act Cap 84. The requirements somewhat vary making it cumbersome to companies.

5.2.4 More Power of Investigation to Capital Markets Authority

In the USA, Congress gave SEC the power to supplement the securities statutes with various rules and regulations. Congress also gave the SEC more power to investigate alleged violations of the securities laws and to bring civil actions against suspected violators. Most insider trading actions are handled by the SEC's Division of Enforcement which is the litigation arm of the SEC. Experienced and technically competent personnel should be appointed by the Capital Markets Authority at competitive salary. Government pay packet has been found to be not attractive enough to attract best talents in the securities industries. In the last couple of years, we have found a large scale of complex securities transactions and the sophisticated fraudulent schemes adopted by unscrupulous operators.

Moreover, the Capital Markets Authority does not have any explicit powers to check money laundering and cross-border violations. The Capital Markets Authority has to depend frequently on investigating agencies like the Police for completion of inquiries. Therefore, to avoid duplication of effort and loss of crucial time in bringing the guilty to book, the Capital Markets Authority needs more power of investigation including (i) power of search and seizure

(ii) inspection, investigation, surveillance and enforcement powers and (iii) implementation of an effective compliance programme.

5.2.5 Advanced software and strong surveillance mechanism to detect insider trading

The SEC and the London Stock Exchange (LSE) use highly advanced software called EDGAR-Electronic Data Gathering, Analysis and Retrieval system which is quite effective in tracking down the manipulators. The Capital Markets Authority needs to be equipped with such high tech software for curbing insider trading. Given the size, complexities and level of technical sophistication of the markets, the tasks of information gathering and analysis of data or information are divided among exchanges, depositories. Information relating to price and volume movements in the market, broker positions, risk management, settlement process and

compliance pertaining to listing agreement are monitored by the exchanges on a real time basis as part of their self- regulatory function. I do suggest improvement of quality and committed people at market- competitive compensation package. Like NASDAQ and LSE, Ugandan stock exchanges should introduce strong surveillance mechanism to detect insider trading.

It is commendable that Uganda recognised that insider trading ought to be discouraged in order to increase confidence in Uganda's securities markets. The researcher notes the following weaknesses in the insider trading legislation and recommends legislative intervention.

While the Act[133] states that an insider shall not cause or procure any person to deal in the securities, the prohibition does not extend to an insider who discourages another person from dealing in the company's securities. The researcher recommends that the Act be amended to include a prohibition of disclosure of information for purposes of causing a person to refrain from trading. This is because it is unfair to the rest of the market participants who may trade, where those with inside information may refrain from trading on the basis of that information thereby avoiding a loss.

There are inconsistencies between the Capital Markets Authority Act and the Uganda securities Exchange limited insider trading Rules as one may not be an insider under the Act but may be so under the Rules. For instance under Rule 2(d) of the Rules, an insider includes a person who obtains inside information from one who would be connected to the company. Thus the rules do not distinguish between a primary insider and a secondary insider. The researcher recommends that the rules be amended to follow the information connected approach of insider trading and that there be more consistency generally between the Rules and the Act.

The exemptions and defences under Uganda's insider trading legislation ought to be widened so that legitimate and important transactions are not barred from being carried out otherwise the operations of the stock market risk being hindered. Exemptions in other jurisdictions include underwriters who may purchase shares pursuant to an underwriting agreement, persons disclosing information in the course of a takeover transaction or a company officials revealing certain information in fulfilment of a statutory obligations[134]and research based on public data. These exemptions ought to be a part of Uganda's legislation. It should also be a

133 Capital Markets Authority Act Cap 84, section 88(4)
134 Section 104B of the Corporations Act, 2001, (Australia)

defence to say that the information was no longer inside information but was indeed generally available to the public. In other jurisdictions, an insider may show that he would have dealt even if he had not received inside information[135]and a defendant may specifically show that trade plan pre-existed the possession of inside information. This is because if the information was already generally available to the public, then the person would not have traded on the basis of inside information, which by definition is information that is generally not available to the public. This defence would be relevant in the Uganda's insider trading legislation.

Requiring connections to the company creates an onerous burden to prosecute a perpetrator of the offence since they will have to prove this connection.[136] Thus it is easier to avoid the prohibition by covering up any link between the perpetrator and the source of his or her information. Kenya has adopted this approach under Section 32A(c) of the Capital Markets Act chapter 485A which defines an insider as a person who is in possession of price sensitive information. The researcher recommends that the law be amended to prohibit insider trading by anyone who possesses inside information regardless of whether they are connected to the company or not since it is the use of information rather than connection between a person and a corporation which should be the basis for determining whether insider trading has occurred.

The law provides that there must have been a conviction before an aggrieved person can bring a civil claim for compensation since the Act provides that a person convicted of a criminal offence is liable to pay compensation. Under the current insider trading legislation, the burden of proving insider trading offences is proof beyond reasonable doubt. The insider trading legislation ought to be amended so that the civil liability does not depend on the criminal liability of a convicted person.

135 Criminal Justice Act, section 53(2)(United Kingdom)
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