

The Legislative Evolution of Insider Trading Law in Pakistan

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Abstract

Inside information abuse has caused enormous damage to the Pakistani financial market. To curb and curtail different legal instruments have been promulgated. This research aims to provide an overview of the legislative evolution of insider trading laws. It analyzes different enactments and their distinct features. The prime issues for inquiry include, how the insider trading law has evolved in Pakistan? How different enactments contributed to the present legal framework? The main focused laws are SEO 1969 and Securities act 2015 as both these directly dealt with the insider dealing prohibition and sanctions. The qualitative research methodology is adopted for subject study. The main objective of this investigation is to explore the varying approaches and tools utilized by the state to curb market manipulation by inside information abuse. SEO 1969 was enacted in the backdrop of several stock market crashes to control the inside information abuse. While the Securities Act was enacted to streamline the legal regime and bring a restructured code to control market manipulation. The research concludes, both subject legislations lack the international standards and end up being toothless legislative devices to curtail the menace.

Keywords: Insider Trading, SEO 1969, Securities Act 2015, SECP, Information Abuse.

1. Introduction

Controversy and humiliation have always been associated with insider trading and in several incidents, it has damaged the reputations in the corporate world. Incidents relating to inside information abuse have always

made great stir in electronic and print media.¹ It triggers detriment, as inside information abuse benefits an already fortunate minority partial gain or upper hand as compared to common shareholders in greater numbers. This minority is already privileged to have access to this information which the majority does not have. The use of this privileged information to avoid loss or earn benefit is legally and morally unacceptable.²

The most common violation of law in capital markets is inside information abuse. It is one of the most popular doctrines of the corporate regime, among lawyers and economic experts equally. As Bainbridge maintains that inside information abuse tops the list of crime thriller plots, inspired by different legal regimes.³ For an efficient market to have a good reputation and smooth working, it is compulsory to prevent inside trading altogether. In Pakistan, the growing complexity in the economy led to a situation of inadequacy of the laws regulating insider trading. The financial market in Pakistan needs to eradicate market manipulation of any kind to survive in the global scenario. This study has focused on the legislative measures to deal with inside information abuse. It is a brief case study on the matter and the inadequacies in the existing laws. In the end the most recent legal developments have been discussed.

The exploration of existing literature on insider information abuse particularly in Pakistan reveals that a comprehensive study to observe the

¹ Insider Trading and other Market Abuses (Including the Effective Management of Price Sensitive Information) E-booklet available at <https://www.jse.co.za/content/JSERulesPoliciesandRegulationItems/Insider%20Trading%20Booklet.pdf>

² Ibid.

³ Stephen M. Bainbridge, An Overview of Insider Trading Law and Policy: An Introduction to the Insider Trading Research Handbook, (Edward Elgar Publishing Ltd, 2013), Electronic copy available at: <http://ssrn.com/abstract=2141457> (Last Accessed January, 2016).

legislative trends is required. *The Law of Insider Trading in Pakistan*⁴ by Samia Maqbool Niazi is a book which deals with the issue in depth. This book deals with the scope of insider trading, the debate of regulating and deregulating, and the law of insider trading in different jurisdictions like the USA, UK, and India in detail. The famous debate on regulation and deregulation has been dealt with sophistication and briefly. The most significant feature of this book is the manner, in which a comparative analysis of different jurisdictions has been presented. This study revealed several technical inconsistencies such as chapter II of guidelines prohibit the associated person from insider trading but not the insider.⁵ But this book analyzed the insider trading laws prevailing under SEO 1969 while with the latest developments in anti-insider information abuse legislation (Securities Act, 2015) there is wide scope for feasibility of another in depth study to analyze the present-day legal instruments.

An empirical analysis conducted by Nuno Fernandes and Miguel exhibits an obvious pattern of price fluctuation in the securities market due to market manipulation and insider trading. Though this research by Nuno Fernandes and Miguel in “Insider Trading Laws and Stock Price Informativeness”⁶ is technically more from an economic background but it does provide a good understanding of insider information trading laws’ impact on stock market. These authors investigated the impact of Insider information laws on the stock market of 48 countries when these laws were enacted for the first time. This study dealt with developed and emerging

⁴Samia Maqbool Niazi, *The Law of Insider Trading in Pakistan* (Federal Law House, 2007), 56.

⁵ Listed Companies Guidelines (Prohibition of Insider Trading) issued at Islamabad on 27th March 2000. Available http://www.secp.gov.pk/Guides/Guide_Listing_Companies_Initial_Public_Offerings.pdf.

⁶Nuno Fernandes, Miguel A. Ferreira, Insider Trading Laws and Stock Price Informativeness, *The Review of Financial Studies* 22, no. 5, (2009), 1845-1887, <https://doi.org/10.1093/rfs/hhn066>.

markets separately. This adds another significant aspect which can be helpful to understand the impact of insider information laws on Karachi Stock exchange. Insider trading laws first emerged in the USA and later adopted by the rest of the world. It is of great importance to study Pakistani laws in context of the doctrines coined in the USA. Another study “Unchecked Intermediaries: Price Manipulation in an Emerging Stock Market” conducted by Khwaja and Mian deals with market manipulation in an emerging Stock market⁷ with a special perspective of intermediaries’ role in market manipulation deals mainly with economic and financial aspects but indeed provided a fair idea of market manipulation practices in Pakistan specially related to price manipulation. This study concludes that more than 44% of brokers' earnings are from manipulative practices and brokers are directly related to private information trading in the stock market. The available data provides insight on the existing legal structure and sets the parameters to evaluate the framework.

1. Pakistan Insider Information Abuse Legislation

Market manipulation control is the most significant aspect of corporate governance. There are a handful of laws and regulations to deal with corporate governance in Pakistan. Some of the major laws are being mentioned here.

- a. Companies Ordinance 2016⁸ replaced by Companies Act 2017,⁹

⁷Asim Ijaz Khwaja, Atif Mian, “Unchecked Intermediaries: Price Manipulation in an Emerging Stock Market”. *Journal Of Financial Economics* 78, no. 1 (2005): 203-241.

⁸Companies Ordinance, (2016) available at <https://www.secp.gov.pk/document/companies-ordinance-2016/?wpdmdl=21214>- (Last accessed December 2016).

⁹The Companies Act, (2017) available at <https://www.secp.gov.pk/document/the-companies-act-2017-updated-18-aug-2022/?wpdmdl=45422&refresh=63fba594770a11677436308> (Last Accessed February, 2022).

- b. Securities and Exchange Ordinance, 1969¹⁰
- c. Income Tax Ordinance 2001¹¹
- d. Listing Regulations
- e. Central Depository Act, 1997¹²
- f. Code of Corporate Governance, 2002¹³.
- g. Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Regulations, 2008
- h. Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Regulations, 2008¹⁴
- i. The Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Ordinance 2002 (Takeovers Ordinance).
- j. Listed Companies (Prohibition of Insiders Trading) Guidelines 2001.

In 2015 and 2016 some new regulations have been included to govern the securities market these are as follows:

- k. Reporting and Disclosure (of Shareholding by Directors, Executive Officers and
- l. Substantial Shareholders in Listed Companies) Regulations, 2015¹⁵

¹⁰Securities and Exchange Ordinance, (1969), available at <https://www.secp.gov.pk/document/companies-ordinance-2016/?wpdmdl=21214> . (Last accessed May 2016).

¹¹Income Tax Ordinance (2001), available at [http://download1.fbr.gov.pk/Docs/2014101313102634216I.T.Ord,2001\(updated\)AmendedJune2014.pdf](http://download1.fbr.gov.pk/Docs/2014101313102634216I.T.Ord,2001(updated)AmendedJune2014.pdf) (Last accessed May 2016).

¹²Central Depository Act, (1997), available at <http://www.na.gov.pk/uploads/documents/Central-Depositories-Act-1997.pdf>. (Last accessed April 2016).

¹³Code of Corporate Governance, (2002), available at <https://www.secp.gov.pk/document/code-of-corporate-governance-2012-amended-july-2014/?wpdmdl=1472>. (Last accessed April 2016).

¹⁴Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Regulations, (2008), available at <https://www.secp.gov.pk/document/listed-companies-substantial-acquisition-of-voting-shares-and-takeovers-regulations-2008/> (Last Accessed April 2016).

¹⁵ Reporting and Disclosure (of Shareholding by Directors, Executive Officers and Substantial Shareholders in Listed Companies) Regulations, (2015), available at <https://www.secp.gov.pk/document/reporting-and-Disclosure-of-shareholding-by->

- m. Central Depositories (Licensing and Operations) Regulations, 2016¹⁶
- n. Securities Brokers (Licensing and Operations) Regulations 2016¹⁷

Most of these laws directly or indirectly deal with insider information abuse. After the 2000 Stock Exchange crash, the SECP¹⁸ adopted Chapter III-A¹⁹ along with the Listed Companies guidelines²⁰ in the SEO 1969. The purpose was to curtail insider information abuse by ensuring a flawless information generation and circulation mechanism, to save investors from any deceptive practices. The need to legislate was acute. The most initial step to control this fraudulent practice in securities market was amendment in Finance Act 1995²¹ which subsequently became part of Securities and exchange ordinance (SECO 1969). Both of these acts constitute the foundations of Pakistani legal regime on Inside Information abuse. Along with this ordinance, Listed Companies (Prohibition of Insider Trading) Guidelines 2000²² were also issued.

The SECO 1969 has some major goals to provide market participants data regarding financial status of issuers, and to prohibit deception, falsifications, and other malpractices in the securities market.

directors-executive-officers-and-substantial-shareholders-in-listed-companies-regulations-2015/?wpdmdl=713 (last accessed June 2016).

¹⁶ Central Depositories (Licensing and Operations) Regulations, (2016), available at <https://www.secp.gov.pk/document/central-depositories-licensing-and-operations-regulations-2016/?wpdmdl=699> (Last accessed July 2016).

¹⁷ Securities Brokers (Licensing and Operations) Regulations (2016), available at <https://www.secp.gov.pk/document/securities-brokers-licensing-and-operations-regulations-2016/?wpdmdl=14922>. (Last accessed July 2016).

¹⁸ Securities and Exchange Commission of Pakistan.

¹⁹ Securities and Exchange Ordinance, (Ordinance No. XVII of 1969) (28 June 1969 as amended up to 2012) available at <http://www.secp.gov.pk/laws/ordinances/>.

²⁰ Listed Companies Guidelines (Prohibition of Insider Trading) (2000).

²¹ Finance Act (1995), available at http://www.na.gov.pk/uploads/documents/1329725424_374.pdf.

²² Listed Companies (Prohibition of Insiders Trading) Guidelines, (2001) available at <http://www.secp.gov.pk/document/listed-companies-prohibition-of-insider-trading-guidelines/>.

Thus, every direct legislation of Pakistan on insider information abuse or Insider Trading with its amendments can be summarized like this:

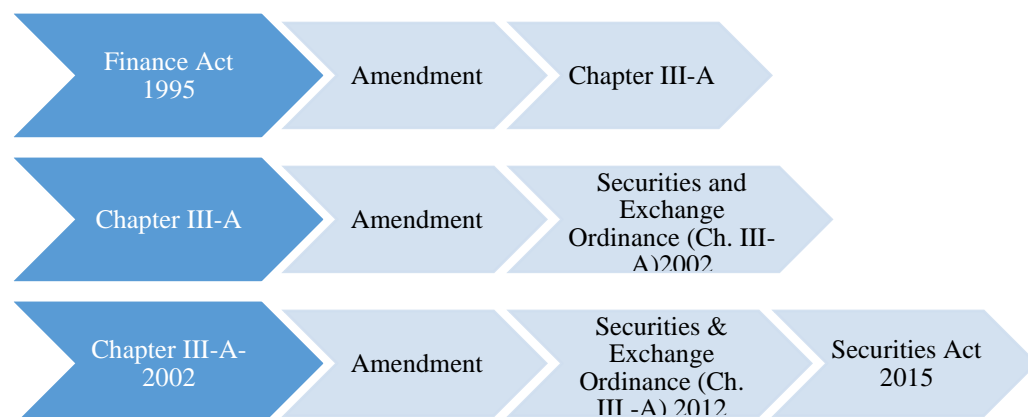


Figure 1 Development of Insider Trading Law in Pakistani Laws.

However, these statutes and guidelines could not serve the purpose effectively. International Monetary Fund published a country report (2004)²³ which maintained that the SECP has initiated the laws dealing with disclosure requirements and inside information abuse. In 2005 a task force²⁴ was constituted to investigate the causes and factors of the Stock Market crisis. The findings of this report maintain that insider information and deceptive devices are widespread in the securities market. In 2005²⁵, 2008²⁶,

²³ International Monetary Fund, IMF Country Report No.04/215 Pakistan: Financial System Stability Assessment, including Reports on the observance of Standards and Codes on the following topics: Monetary and Financial Policy Transparency, Banking Supervision, and Securities Regulation (July 2004). Available at: <https://www.imf.org/external/pubs/ft/scr/2004/cr04215.pdf>. (Last Accessed January 2016).

²⁴ SECP, Report of the Taskforce: Review of the Stock Market Situation March 2005, Available at: <https://www.secp.gov.pk/document/stock-market-task-force-report-2005/>. (Last Accessed January 2016).

²⁵ Atiya Y. Javed, "Stock Market Reaction to Catastrophic Shock: Evidence from Listed Pakistani Firms, PIDE Working Papers (2007:37) Pakistan Institute of Development Economics, Islamabad.

²⁶ Stock Market Crash, Press release by SECP available at <https://www.secp.gov.pk/wp-content/uploads/2016/05/recommendations-of-study-of-2008-stock-market-crisis.pdf>. Last Accessed March 2022.

2009 and 2017²⁷ and, 2020²⁸ Karachi Stock Market crashed several times. Meanwhile the watchdog experienced some significant cases of Insider information abuse. This catalyzed the need for new legislation to address this significant issue resulting in Securities Act 2015.

2. The Chronological Order

As insider information has the tendency to directly affect the securities market, legislative measures are being taken around the globe to prevent its illegal use by insiders. In Pakistan the first step towards addressing the issue was amendment in Finance Act 1995 as Chapter III-A was introduced in Securities and Finance Ordinance, 1969.

Along with this ordinance, regulator (SECP) promulgated Listed Companies (Prohibition of Insider Trading) Guidelines 2000. Insider information dissemination prohibition law came into limelight after the Stock Market crashed in 2000 as violation of this law was supposed to be the main cause of this financial crisis. In the backdrop of several stock market crashes SECP started the review of the then existing legal provision to curb market manipulation by inside information abuse; the same was recorded by IMF Report (2004).²⁹ As stated above after this crisis, Karachi Stock Market crashed in 2008, 2009.³⁰ All these financial crises and halt in economic growth lit the fire to review the legal provisions in this regard.

²⁷ Salman Siddiqui, "Pakistan's Stock Market: From Asia's Best to Asia's Worst", *Express Tribune*, December 19, 2017.

²⁸ Amir Latif, 'Pakistan Stock Exchange Loses 1,200 Points', *Asia Pacific*, International edition, accessed 2021, <https://www.aa.com.tr/en/asia-pacific/pakistan-stock-exchange-loses-1-200-points/1723218>.

²⁹ International Monetary Fund, IMF Country Report No.04/215 Pakistan: Financial System Stability Assessment, including Reports on the observance of Standards and Codes on the following topics: Monetary and Financial Policy Transparency, Banking Supervision, and Securities Regulation (July 2004).

³⁰ See note 26, 27.

In all these years several cases arose as whistleblowers. Some significant cases include Pakistan Kuwait Investment Company, Jahangir Siddiqui Group (JS Group),³¹ Aqeel Karim Dhedhi (AKD) and Dawood Capital Management Company.³² They were investigated and penalized by the SECP in recent years. These facts and figures compelled an up-gradation in the existing system to cater the issue. In January 2015 a government Bill named Securities Act 2015 was passed by Senate of Pakistan³³ aimed to remove gaps in the previous laws. Securities Act 2015 is one of the most awaited and anticipated legislation, more extensive than its predecessor. It is intended to eliminate inadequacies, lacunas in the 1969 SEO, and to reform the grey areas in the law. It will bring an exhaustive, broad, and ample regulation. Key issues addressed in this law are strict prerequisites of accreditation for all market participants inclusive of the exchanges, the clearing company, the CDC, stock dealers, intermediaries, syndicates, mediators, prevention of Inside Information abuse and deceptive and manipulative techniques.³⁴

3. Inadequacy of Legal Provisions SEO 1969

Some major deficiencies in the Securities and Exchange Ordinance, 1969,³⁵ are lack of duties imposed on securities exchange, no audit of the listing authorities/entities, inadequate authority of powers of regulator for

³¹Press Released by SECP at

http://www.secp.gov.pk/news/PDF/News_13/PR2_April24_2013.pdf.

³² Before the Executive Director (Securities Market Division) in the matter of Show Cause Notice No. SCD-SD (Enf)/khi/dcml/2013/061 dated March 22, 2013 issued to M/S Dawood Capital, pdf available at http://www.secp.gov.pk/orders/pdf/Orders_2013/19_Order_SCN-DCML.pdf (Last Accessed May 6th, 2015.)

³³ Act Available at <http://www.senate.gov.pk/en/index.php> (Last accessed May 6th, 2015).

³⁴ Ibid.

³⁵ Securities and Exchange Ordinance, 1969 (Ordinance No. XVII of 1969) (28 June 1969 as amended up to 2012) available at <http://www.secp.gov.pk/laws/ordinances>.

stakeholder in investment sector, rules regarding clearing houses, admissibility requirements and duties of clearing house, central depository, a deficient arrangement for investor complaints, inadequate rules and regulations for the regulating authority.

Major deficiencies in Securities and Exchange Ordinance, 1969³⁶ revealed that there are insufficient provisions regarding eligibility criteria of stock exchanges, financial reporting, inquiries, scrutiny, and rules for judicial inquiry, information abuse and entities functional without license³⁷. The continuous rise of stock market crisis and crashes give rise to questions about the efficiency of the regulator and concerned laws and regulations as well. Inside information abuse law has several shortcomings. Stockbrokers are indulged in fraudulent sales and in inside dealings as well. A number of incidents brought the issue of insider trading into limelight.

4.1 Civil Liability for Insider Trading

In SEO 1969 only civil liabilities have been imposed on the offender. Section 15 E defines the liabilities for contravention from Section 15 which prohibits insider trading. The section³⁸ is being reproduced here.

15E. *Liability for contravention.* — (1) anyone who infringes 15A (1) shall be liable to fine. This fine may range from 10 million rupees to increasing the magnitude of the profit three times or made loss evaded by said person, or the magnitude of loss incurred by the victim, the amount higher will be imposed on the offender or loss suffered by another person,

³⁶ Ibid.

³⁷ Ibid.

³⁸ Section 15 E, Securities and Exchange Ordinance, 1969 (Ordinance No. XVII of 1969) (28 June 1969 as amended up to 2012), S15. <http://www.secp.gov.pk/laws/ordinances>.

whichever amount is higher.

(2) Additionally with the fine 15 A (1), the said person, –

- a. may be directed by the Regulator,
 - (i) to submit to the regulator, equal amount of money to the profit or loss by the said person.
 - (ii) to pay the victim or sufferer, the damage beard by that person. and
- b. may, if the contravening person is among the executives in management, finance, audit, consultancy of a listed issuer, be dismissed by an order of regulator and embargo of 3 years from auditing any public company will be imposed.
- c. may, if said person in an intermediary registered in the securities exchange, his license will be concealed.

(3) if an insider reveals Inside Information to any one not mandated to possess this information, the insider shall be predisposed to fine, levied by the regulator, extending to thirty million rupees.

(4) The Regulator may, through announcement in official Gazette, formulate e regulations for persons who generate or circulate research regarding listed securities or issuers of these securities and persons who control the flow of information endorsing or proposing investment strategy, intended for distribution channels or for the general public.³⁹

This section contains civil liabilities for contravention from the law, which include a fine ranging from ten to thirty million rupees, to pay any amount gained through inside dealing or any evaded harm and expulsion from

³⁹Ibid.

office. No criminal liabilities have been provided in this ordinance.⁴⁰ Insider trading is known as white collar crime worldwide and mostly criminal penalties are included with civil liabilities. Absence of criminal penalties for insider trading is an anomaly.⁴¹ For all persons indulging in Inside Information abuse not only civil rather criminal sanctions must be provided.

4.2 Market Manipulation and Inside Dealing in SEO 1969

In most of the legal regimes market manipulation and insider trading has been linked together. Inside dealing is considered a kind of market manipulation or at least both these fall under market abuse which are linked together. In SEO 1969, Section 15 of Chapter III-A deals with insider trading and section 17 and 18 of chapter IV deals with other market manipulation practices. Like the rest of the world, both relevant provisions must be linked which will enhance the mechanism of their implementation. Moreover, this issue existed in the SEO 1969 amendment in 2002 as well.⁴² Now is the time to bring the law in harmony with the rest of the insider trading regimes. This would not become a mere tool to harmonize the national law with the rest of the world, but it will enhance efficiency and understanding. From financial and economic perspective both market manipulation and insider trading are inter linked thus a linkage from legal point of view will bring more coherence in law.

4.3 Liabilities of Intermediaries in SEO 1969

Intermediaries play a vital role in the securities market. With respect to insider trading the most important issue is their indulgence in the deals potentially backed by inside information abuse. The perks of indulging in

⁴⁰ Ibid.

⁴¹ Niazi, *The Law of Insider Trading in Pakistan*, 79.

⁴² Ibid., 77.

these transactions include associated commission, receipt of good name in the market and addition in clientage. To curtail these practices some regulators have imposed prohibitions on intermediaries to avoid any transaction which seems to include inside information abuse and proper sanctions are imposed in case of violation of these rules.

Danish legislation sets a decent example by maintaining a fair ground for legitimate trade and prohibiting any aiding or abetting the insider trading,⁴³ it imposes a duty on securities dealers that if the person desirous of any transaction knows or is assumed to know inside information no transaction be carried out. Along with it the securities dealer has been obliged to⁴⁴ inform the concerned authority regarding any trading activity which amounts to inside information abuse.

All these factors highlighted the need of a new legal regime to address these issues effectively. Resultantly, the Pakistani legislature passed a new securities law in 2015.⁴⁵ Main concern here is “Insider information Abuse” prohibition. This new legislation of prohibition of insider information abuse is not exhaustive. Some of the major flaws and inadequacies are being discussed here.

4.4 Recent Legal Developments

Chapter III-A of Securities ordinance 1969 dealt with Inside Information abuse in the securities market. As cited previously, along with this law SECP issued guidelines for listed companies. But both these enactments did

⁴³ IOSCO report on Insider Trading legislation” Insider Trading how Jurisdiction regulate it” by International Organization Of Securities Commissions available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf> (Last accessed February, 2016).

⁴⁴ Securities Trading, etc. Act (2008), sec. 3 (6) of Denmark available at https://www.finanstilsynet.dk/upload/finanstilsynet/mediafiles/newdoc/acts/cact214_020408_new.pdf

⁴⁵ Securities Act, (2015) available at <http://www.secp.gov.pk/laws/acts/>

not serve the purpose. There were several contradictions between the sections of SEO 1969 and the SECP guidelines. Some of which include person associated and person connected inconsistency and insider himself not prohibited from insider dealing. With the passage of time, it was realized that a more efficient, comprehensive, and exhaustive legislation is needed to overcome the inadequacies of existing law. In this scenario the first milestone was 2012 amendments which addressed some of the essential issues. Like any other law it was not perfect so in 2015 national assembly passed the most awaited and anticipated Securities Bill 2015. This is certainly an extensive piece of legislation.

This law deals with several matters about listed securities activities, procedures for issuers, accounting, and assessment; market mediators, prerequisites, accreditation, registration and licenses, authority, and jurisdiction of the commission to issue guidelines, conduct, control and inspect, code of conduct,⁴⁶ professional comportment procedures, issuance of contract note, and financial autonomy. This Act has dealt with important issues like subscription offer, take-overs, inside information abuse, disclosure in prospectus and required material, impartiality of expert-statement, criminal and civil sanction and liabilities, disclosure by public companies, market manipulation and legislative authority assigned to the regulator.⁴⁷

Moreover, the legislation deals with malpractices in market, contravention of law, supervision and investigation, intercession powers of commission, whitewash, painting the tape/ runs, artificial heavy trading, improper matched orders: advancing the bid, pumping, and dumping, liability in case of damages, authority to check any information,

⁴⁶ Ibid., Part VI.

⁴⁷ Ibid., Part X.

examination, assessment, investigation substantive and procedural authority in this regard. This act targets to eliminate the grey areas and lacunas in the 1969 SEO. The new enactment intends to restructure the existing framework and rectify the anomalies in the law. A comprehensive, inclusive, and broad regulation is intended which will address several significant issues by providing provisions for proposing prerequisites of accreditation of market intermediaries including the stock exchanges,⁴⁸ the clearing company,⁴⁹ the CDC, stockbrokers, agents of stockbrokers, underwriters, balloters, transfer agents etc.

It aims to provide fundamentals and preconditions for all entities credited under this law, rules of business and a strict compliance standard for perpetual financial markets. In a briefing to print and electronic media the SECP Chairman claimed that this new Act will provide a much operative and implementation-oriented regime. It will delegate an increased authority for severe punitive action against any contravention of law, comprising a variety of penalties. The new law also has thorough provisions⁵⁰ regarding roles and liability of stock exchanges, CDC, clearing houses, any inside information abuse, market manipulation remedies and penalties, legislative authority to prevent money laundering, regulating business of brokers, securities advisors and analysts and their conduct as well.

4. The Securities Act 2015

The Securities Act 2015 was promulgated at once after being passed from the parliament Except for Part V “Regulated Securities Activities” to be implemented whenever a date was announced by the parliament. A critical

⁴⁸ Securities Act (2015), Part II, available at <http://www.secp.gov.pk/laws/acts/>.

⁴⁹ Ibid, part IV.

⁵⁰ Ibid.

analysis brings forth the shortcomings as no extension in existing provisions concerning prohibition of insider information disseminating or divulging prevails. If this act is compared with prevailing laws around the globe, it becomes evident that several basic and vital elements are missing. Civil as well as criminal liabilities are imposed⁵¹ on insiders involved in trading private information in most of the jurisdictions, but the imposition of penalties to create deterrence have not been adopted in the mentioned recent legislation.

5.1 A Legitimate Disclosure of information

Legitimate disclosure of information is a necessary evil. Although this can complicate the efforts to curb and curtail the practices of insider information abuse. Section 131 deals with legitimate disclosure of information. Though no specific persons are mentioned, this section directs to the professionals who receive sensitive information in the ordinary business practices. A positive thing to note here is that the law backs any disclosure of information to specific persons, by a mandatory public disclosure of information. There are some exceptions required by the business and market practices worldwide. Same exceptions are provided in this section as well.

Moreover, Section 131(2) and 131(3) impose a duty on listed companies to provide a complete list of persons who have connection to the flow of privileged information to the commission. This data shall be updated regularly. This list is supposed to mention that the persons in the list hereby acknowledge the fact that they are prohibited from using any inside information for personal gains or advising or tipping anyone else.

This is another significant step to prevent Inside Information abuse

⁵¹ Ibid.

as it mitigates the plea of not intended inside information abuse and leaves no room behind for the culprit. As Huge et al⁵² describe that when the disclosure per unit time increases the expected profits of an insider decreases as even to half of the expected profits before disclosure. So, disclosure of information not only moderates trading costs but brings market efficiency as well.

5.2 Insider Information

Definition of “Insider information” is the pivotal point of all legislative measures to address insider information abuse. The broad and vivid definition will enhance the efficiency of the control system.⁵³ To deal with this important pillar of insider trading legislation a section from Pakistani Law is being described here. Insider Information is defined in Section 129 of the Act⁵⁴ as,

- a. Any information of the nature, which is not publicized, but concerning, in any direct or indirect manner, to public listed company or companies and about their stock, if this information is announced it may have an impact on the value of listed stock or the value of other listed stock in the securities market.
- b. Any information about derivatives on commodities, which is nonpublic, concerning one or more derivatives.
- c. concerning senior executive officers who decide in lieu of listed stock, any information regarding a communication between these persons and any clients or investors and about any directions about

⁵² Steven Huddart, John S. Hughes and Carolyn B. Levine, “Public Disclosure and Dissimulation of Insider Trades”, *Econometrica* 69, no. 3 (May,2001):665-681, available at <http://www.jstor.org/stable/2692205> (Last accessed 25-03-2016)

⁵³ Stephen Herne, “Inside Information: Definitions in Australia, Canada, the U.K., and the U.S”. *Journal of International Law* 8, no. 1 (1986), available at <http://scholarship.law.upenn.edu/jil>. Last Accessed March,2016.

⁵⁴Securities Act (2015), sec. 129, (Part XI).

transactions in securities or

- d. Any Information concerning future transactions of a person in securities or any decision to trade.⁵⁵

For the occurrence of information abuse, the section provides following elements to be present:

- (i) Information, which is not made public,
- (ii) Information about listed securities and derivatives on commodities,
- (iii) Information about intermediaries and any other person's transactions in future,
- (iv) Information which will have an effect on the price of listed securities.

Insider information-definition has a very significant role in legislation to prevent insider trading. There are some points emphasized by the International Organization⁵⁶ in a report⁵⁷ regarding inside dealing laws in different jurisdictions. The IOSCO report⁵⁸ has mentioned that mainly two issues are to be addressed by the regulator while legislating about insider trading. These issues are confidentiality and materiality.⁵⁹

⁵⁵ Securities Act (2015), sec. 129, (Part XI).

⁵⁶ International Organization of Securities Commissions (IOSCO).

⁵⁷ IOSCO report on Insider Trading legislation" Insider Trading how Jurisdiction regulate it".

⁵⁸ IOSCO report on Insider Trading legislation" Insider Trading how Jurisdiction regulate it" by International Organization of Securities Commissions available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD145.pdf> (Last accessed February, 2016).

⁵⁹ Francis J. Burke, Jr, Steptoe & Johnson, "Insider Trading Securities Violations", ABA Section of Litigation 2012 Corporate Counsel, CLE Seminar (2012) available at

Both confidentiality and materiality can be considered as elements of “Inside Information” definition. These have been broken down into more basic points which will be discussed further in detail. A simple categorization is being provided below for better understanding.

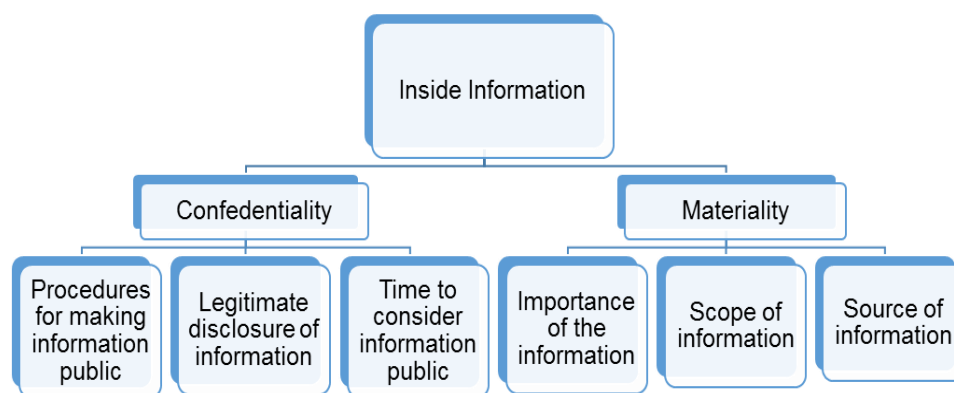


Figure 2 Elements of Inside Information Definition

Both these elements have specific details to be analyzed further. The IESCO standards of legislation and other international jurisdictions’ legislative standards go far beyond the securities Act 2015.

5. Comparison of Securities Act 2015 & SEO 1969

Here a brief comparison of SEO 1969⁶⁰ and Securities Act⁶¹ 2015 will be done. Along with it the features of insider trading legislation will be described in a manner that exposes the loopholes in Pakistani legislation.

In Securities Ordinance 1969 some of the problems were lack of

http://www.americanbar.org/content/dam/aba/administrative/litigation/materials/2014_women/written_materials/b4_1_insider_trading_securities_violations.authcheckdam.pdf

⁶⁰ Securities and Exchange Ordinance, (1969) (Ordinance No. XVII of 1969) (28 June 1969 as amended up to 2012) available at <http://www.secp.gov.pk/laws/ordinances/>.

⁶¹ Securities Act, 2015.

criminal penalties, a lack of linkage between market manipulation and insider trading, no measure to forbid intermediaries from insider trading. All these are still there in Securities Act 2015 except criminal liabilities. This comparison can be best presented in a tabular form hence below is the table to explain this comparison.

Features	SEO 1969	Securities Act 2015
Civil Liabilities	✓	✓
Criminal Liabilities	X	✓
Market manipulation and Insider Trading linked together	X	X
Obligations on Intermediaries	X	X
Tender Offer setting addressed	X	X
Time to consider information public	X	X
Disclosure procedure available	X	X

Table 2 A comparison of SEO 1969 and Securities Act 2015.

Interestingly SEO 1969 was enacted in the backdrop of several stock market crashes to control the inside information abuse. While the Securities Act was enacted to streamline the legal regime and bring a restructured code to control market manipulation. Both legislations lack the international standards and end up being toothless legislative devices to curtail the menace.

6. A Critique of Current Pakistani Legal Regime on Insider Trading

Some of the salient features of the new legislation have been discussed already. Now a critique of Securities Act 2015 is being presented in the light

of above discussion. Analysis of Inside Information definition as available in Securities Act 2015 does not even mention some very essential terms. The term ‘material’ is presumed to be a vital part of inside information definition; however, this is missing from the said law.⁶² Along with it any signal towards precise or specific information is not present in the act. Any attribution towards materiality of information with regard to its scope, impact or importance is not available. Other significant issues connected to insider trading are procedures required to consider information public and the essential time to consider information public. Any of these issues are not addressed in the new legal regime.

For identifying insiders, the connected person approach is adopted but it lacks a broad view hence fails to include temporary and accidental insiders. This causes grave difficulty while prosecuting these insiders. The study revealed the insider trading regime is inclined towards a broader approach of defining insiders, inside information and related elements. The Pakistani financial market is at the verge of an online or internet-based revolution in securities trading. For simplification and efficiency, a connection information approach with a blend of connected person approach will be the best possibility.⁶³ As compared to only a person connection approach a balanced approach with features of both will be more result oriented.⁶⁴ In this approach listing of all possible connected persons and providing exemptions wisely will be the core issue.⁶⁵ Some jurisdictions have used this approach to deal with this issue. In Singapore

⁶² See section 130 of Securities Act 2015.

⁶³ As in UK and Singapore models.

⁶⁴ The Definition Of “Insider” In Section 3 of the *Securities Markets Act 1988*: A Review and Comparison with Other Jurisdictions, Discussion Paper Series 218, Massey University, School of Accountancy (2003). Available At [Http://www-accountancy.massey.ac.nz/publications.htm](http://www-accountancy.massey.ac.nz/publications.htm)

⁶⁵ Roman Tomasic, James Jackson and Robin Woellner, *Corporations Law: Principles, Policy and Process*, 4th. ed. (Butterworths, Australia :2002) 998.

the connected person list seems very exhaustive. While in UK legislation connected persons' list is not much elaborate moreover, presumption of *mens rea* is not similar as in Singapore.⁶⁶

In terms of prohibited activities, a major lacuna is a very finite and circumscribed scope of legislation. The 2015 legislation is silent on tender offer and intermediaries⁶⁷ for dealing in transactions based on inside information. Tender offer⁶⁸ is a frequently practiced form of trade and is equally prone to inside information abuse, while Pakistani law is silent on this issue altogether. An addition of tender offers in the covered areas of insider dealing law will yield legal consistency and fairness in the market.

Disclosure requirements are included but not exhaustive. Some core issues like minimum time to disclose, medium of disclosure, delaying disclosure of inside information, equivalent information, Publication of information on internet sites are not addressed appropriately.⁶⁹ Additionally, disclosure of trades of BOD members and other insiders are not streamlined to. For defenses, Chinese wall and operations of state must be introduced for fair and just applicability of law.⁷⁰ Furthermore, public companies have not been held liable to incorporate codes for disclosure of information and control of its flow.

7. Conclusion

Some significant observations are being summarized here. The new legislation (Securities Act 2015) is quite an inadequate attempt to govern

⁶⁶ Ibid.

⁶⁷ For details see Securities Act 2015, sec. 130-131.

⁶⁸ Ibid., 132-135.

⁶⁹ Ibid., Part X- XI.

⁷⁰ For details Bradley J. Bondi, Steven D. Lofchie, "The Law of Insider Trading: Legal Theories, Common Defenses, And Best Practices for Ensuring Compliance", *Nyu Journal of Law & Business* 8, (2012), 151. Available at: <http://ssrn.com/abstract=2028459>. (Last Accessed August 2016).

the securities market from inside information abuse. Though long-awaited criminal liabilities have been introduced, still a number of issues are neglected. If provisions of Securities Act are examined in a comparative manner with international practice it becomes evident the law is a mere patch work. Several shortcomings are found with respect to broad approach, enforceability, exhaustive issues to be dealt with. This recent legislation could not answer several crucial questions sufficiently. The gaps existed in SEO 1969-as amended till 2012 are present in the Securities Act 2015. Some of the core issues are a vague definition of inside information and insiders. This definition lacks comprehensiveness in describing the attributes to categorize any information inside information. Inside information definition needs a legislative overhaul.

The criteria to include information within the ‘inside information’ should be widened, amplified and intensified. It will provide a strong foundation to control inside information abuse. Certain key issues of inside information definition need to be dealt with due care in order to bring a compact, comprehensive and exhaustive law to deal with the issue.

Market manipulation has been linked with inside trading in most jurisdictions to bring harmony, consistency, and simplicity. In Pakistani law the same features can be achieved through connecting both these malpractices together. Another significant observation is that no procedural up gradation took place amid new law. A particular time frame to estimate information to be public after its disclosure for proper dissemination of information in the market is a very imperative aspect in insider trading laws. Nonetheless no time frame has been given for publication of information or its dissemination in the market. While imposing the duty to abstain from any indulgence in prohibited activities intermediaries have not been addressed directly and particularly. The Pakistani financial market is in dire

need of investors for a persistent growth. An enhanced mechanism for investor protection and an efficient market will boost the economy eventually.
