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# Insider dealing and Kwarteng's mini-Budget

By Tom Bushnell

**T**he weeks following the then chancellor of the exchequer Kwasi Kwarteng's so-called "mini" Budget' saw a torrent of negative news stories for the UK government.

Among the most striking of these were reports claiming that, during the week prior to the announcement, a group of hedge fund managers attended a dinner after which they 'shorted' the pound and government bonds.

Hedge fund managers reportedly profited from sterling's dramatic plunge in value shortly after the fiscal statement. A separate report alleged Kwarteng attended a champagne reception with hedge fund bosses hours after his announcement.

Questions have been asked over whether this could have led to insider trading. Labour MP Tulip Siddiq asked the Financial Conduct Authority to investigate 'whether it is possible that any leaks or information... contributed to the collapse of the pound'.

Jake Berry, Conservative party chairman, denied to Sky News early in October that the chancellor had given details of future fiscal plans to people at the first event.

But could what has been alleged really point to 'insider dealing'? How does the FCA investigate such matters? And what steps should professional advisers take to ensure they do not fall foul of insider trading law?

## What is insider dealing?

Insider dealing (also known as insider trading) is a criminal offence contrary to Part V of the Criminal Justice Act (CJA) 1993. It is also a regulatory or civil offence under the Market Abuse Regulation.

Allegations of insider trading are investigated by the FCA, which also acts as prosecutor in criminal cases. FCA investigations can be triggered in a number of ways, including by the FCA's own market surveillance systems, suspicious transaction and order reports, whistleblowing or media allegations.

At the heart of insider dealing – whether criminal, regulatory or civil – is the possession of 'inside information', the precise definition of which is crucial to determining whether there is an offence (and is dealt with in detail below).

In broad terms – and subject to various specific defences – anyone who possesses inside information is prohibited from doing any of the following:

- Dealing or trading in relation to the information;
- Encouraging or recommending another person to deal; or
- Disclosing that information (other than in the proper performance of the functions of one's employment/office/profession).

The criminal offence of insider dealing can be tried in either the magistrates' court or Crown Court. In practice, it is always heard in the latter, in front of a jury. Anyone found guilty of insider dealing faces a maximum of 10 years' imprisonment. They can also expect the proceeds of their criminality to be confiscated.

Regulatory misconduct leads to an enforcement process within the FCA, with the possibility of an appeal (a 'referral') to the Upper Tribunal. The FCA can impose a range of sanctions, including significant financial penalties.

## **What is inside information?**

While financial professionals may feel they have a common-sense idea of what constitutes inside information, the term has a closely defined meaning in the criminal law.

Under s. 56 of the CJA 1993, inside information is information that:

*(a) Relates to particular securities or to a particular issuer of securities or to particular issuers of securities and not to securities generally or to issuers of securities generally;*

*(b) Is specific or precise;*

*(c) Has not been made public; and*

*(d) if it were made public would be likely to have a significant effect on the price of any securities.*

Financial professionals need to understand the borders of the definition of inside information in order that they do not stray beyond them. In order to do so, it may be useful to take the above criteria one by one and apply each to the recent "mini" Budget concerns.

### **Does the information relate to particular securities or issuers etc?**

Insider dealing prosecutions usually relate to particular pieces of market activity relating to particular securities or issuers (which can include the UK government and Bank of England). In practice it is often as specific as 'company A is about to announce a takeover of company B'.

Kwarteng's fiscal package dealt with the government's large-scale economic decisions, the likes of which have hitherto not been used as the basis for insider dealing prosecutions. Given that the UK government is an issuer of securities, this would probably not be a major hurdle for any potential prosecution. But macro-economic decisions by the government are less likely to meet the further elements of the definition of inside information.

### **Was the information specific or precise?**

Insider dealing juries are generally left to decide for themselves whether the information in question is 'specific or precise', but the FCA is required to identify exactly what the specific or precise information was.

This is not always straightforward: past insider dealing trials have turned on whether defendants received a ‘rumour’, a ‘tip’ or the fruit of another person’s inspired guesswork – or whether information stepped over the line into something ‘specific or precise’.

General or nebulous hints (such as early information about a chancellor’s macro-economic plans) are unlikely to be sufficient.

### **Was the information not public?**

In order for the FCA to prove information is ‘inside’, it must prove a negative: namely that the information was not public at the relevant time.

In practice, the regulator does this by commissioning market experts to comb open-source publications (such as newspapers and online chatrooms) for the specific piece of information in question. If the information can be shown to have been in the public domain at the relevant time, then a prosecution will fail.

The "mini" Budget allegations might run into two problems here. First, Westminster is notoriously leaky. Second, the fiscal statement came after a Conservative party leadership contest in which Liz Truss talked repeatedly about her economic plans (indeed, supporters of Liz Truss’s leadership rival Rishi Sunak have pointed to specific warnings he made in the campaign about the pound being devalued if Truss did what she was planning). The recipient of information may therefore be able to argue it was already public.

### **Was the information price sensitive?**

In order to be classified as inside information, the information must be price sensitive. This requires expert evidence, with the question for the expert being a hypothetical one: if the information in question had been released to the market at the time of the alleged offence, would it have had a significant effect on the price of any securities?

In practice, experts tend to interpret this as meaning an effect that would not otherwise be accounted for by normal market movements. The fact that the price of securities did move dramatically upon an announcement is often good evidence that the information had been price sensitive.

In the "mini" Budget case, however, any potential prosecutor would have to assess to what extent, if any, the market reacted as it did as a consequence of the government's actions as opposed to other factors that have occurred since (such as the ongoing war in Ukraine or a strong dollar etc).

### **I think I may have inside information, what should I do?**

The criminal law definition of inside information is not simple. Its definition under the Market Abuse Regulation is a little simpler. But it is nonetheless vital that everyone working in financial advice is able to recognise inside information in order that they can behave appropriately when they encounter it.

In practice, issuers of securities and other professionals who handle inside information should have procedures in place to govern its management and dissemination.

A critical aspect of these is the creation of 'insider lists', which identify everyone in possession of the information in question.

Anyone on such a list should be instructed not to trade in relation to the information; not to encourage others to trade; and not to disseminate the information outside of those already in possession of it. Anyone who is uncertain whether they may or may not have inside information should seek clarification, and in the meantime do the same.

Once the information in question is deemed to no longer be 'inside' (for example after a company takeover is announced to the market), then there should be a 'cleansing' process by which the restrictions on the insiders are lifted.

### **How does the FCA investigate insider dealing?**

Allegations of insider dealing are taken seriously by the FCA. The agency has a dedicated enforcement and market oversight division of 625 staff, which includes specialist investigators who work alongside lawyers.

The FCA's most recent data reveal that during the financial year 2021-22 it opened 25 new investigations into insider dealing – the second most common investigatory subject for the agency.

Any FCA investigation into insider dealing is likely to take a long time. While the agency does not break down its data by subject matter, the average length of an FCA criminal investigation is 30 months.

Matters that go to trial are likely to last longer. The agency's most recent insider dealing prosecution, which is due to be retried in September 2023, concerns trading which took place in summer 2016.

### **Will there be a prosecution in the mini-Budget case?**

Based solely on what is publicly known about the "mini" Budget matter, it seems unlikely any FCA investigation would lead to a prosecution.

Even if conversations between government and traders took place (and there is no direct evidence that they did) it is far from certain that what allegedly passed between the parties was inside information as defined in law. Even if it was, the prosecutor would also need to establish the remaining ingredients of one of the three insider dealing offences.

But while a prosecution in this matter may seem unlikely, the FCA does take allegations of insider dealing seriously. It has the resources and expertise, and is willing to strenuously investigate and prosecute insider dealing – work Mark Steward, FCA director of enforcement and market oversight, described in 2021 as "vitaly important".

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