

THE USE WITHOUT RIGHT OF THE PRIVILEGED INFORMATION (INSIDE TRADING) – OFFENSE REGARDING THE CAPITAL MARKET

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Abstract

This study addresses the particularly complex problem caused by one of the offense that can be committed in the capital market. Naturally, the article also includes an introductory analysis of the field and the regulation of the capital market, aspects that complement the premise of all offenses defined by the Law no. 297/2004, but examines in particular one of the incrimination texts regulated by the same normative act. It is about article 279 paragraph b) and article 245 of the Law no. 297/2004 which, without having a marginal designation, was intended to define the offense of unlawful use of the privileged information.

Keywords: capital market, privileged information, offenses regarding the capital market, capital market manipulation

1. Introduction

The capital market field is a highly controversial one because of its novelty in our country, its special technicity it presents, and the seriousness of the offenses already committed within it. For this reason, as well as due to the need to prevent the criminality's import, which is very easy by reference to the specifics of the field, *multiple legislative changes* occurred, with a high celerity which have often determined difficulties in understanding and applying the legal norms, especially the norms of incrimination.

The legislative framework consisted, in turn, in the Law no. 52/1994 regarding securities and stock exchanges, the first with this specific in contemporary Romania, in the Government Emergency Ordinance no. 28/2002 regarding securities, financial investment services and regulated markets, approved with amendments and completions by the Law no. 525/2002, and, currently, in the Law no. 297/2004. This normative act is an ample, complex one, including virtual regulations that came into force at a later moment than the one decided for the entry into force of the Law no.297/2004¹.

As with the previous normative acts, the Law no. 297/2004 as well includes legal norms of incrimination, therefore rules defining crimes². Thus, the article 279 of the Law stipulates : "It is a crime and is punished by imprisonment from 6 months to 5 years and the interdiction of certain rights: a) the deliberate presentation by the administrator, director or executive manager of the company to the shareholders of inaccurate financial statements or unrealistic information about the economic status of the company; b) committing the crimes referred to in articles 245-248; c) intentional access by unauthorized persons of the electronic trading systems, depository or clearing and settlement systems. "

In addition, the article 279¹ of the same normative act states: "Theft of the financial instruments of the customers and / or of the money funds related to them constitutes an offence and is punished in accordance with the provisions of the Criminal Code."

In order to ensure the main rules for the fulfilment of the criminal norms, the Law no. 297/2004 regulates the establishment and the functioning of the financial instruments markets, with their specific institutions and operations, as well as the collective investment bodies, in order to mobilize the financial resources through the investment in financial instruments. This law applies to the above-mentioned activities and operations performed on the Romanian territory. The National Securities Commission is the competent authority that applies the provisions of the special law by exercising the prerogatives established in its statutes. However, the provisions of the Law no. 297/2004 do not apply to money market instruments, regulated by the National Bank of Romania and to government securities issued by the Ministry of Public Finances, if the issuer chooses for trading them a market other than the regulated market defined in article 125.

A *regulated market* is a trading system for financial instruments that:

- a) operates regularly;
- b) is characterized by the fact that the regulations issued and subject the approval of the Romanian National Securities Commission (C.N.V.M.) define the operating conditions, the market access, the conditions for admission to trade a financial instrument;
- c) complies with the reporting and transparency requirements for the protection of the investors being laid down by law as well as with the regulations issued by C.N.V.M. in accordance with EC law.

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¹ Based on article 290 from the Law no. 297/2004, it entered into force 30 days after its publication in the Official Journal of Romania.

² For a thorough analysis of all the crimes (offenses) defined by this normative act, see the chapter drafted by the same author in the collective work: Criminal Law of Business (co-authored by *Al. Boro*), CH Beck Publishing House, Bucharest, 2016.

The provisions of the Law no. 297/2004 do not apply to the management of public debt in which are involved the National Bank of Romania, the central banks of the Member States and other national entities in Member States with similar functions, the Ministry of Public Finances, as well as other public entities.

All offenses defined by the Law no. 297/2004 suppose that those *behaviours described by the incrimination rules must be adopted within or about some operations performed on the capital market. The body with specialized attributions in this field is the Romanian National Securities Commission.*

Originally, the market was the public place in the city where supplies or other items were put up for sale, but through generalisation, currently the market represents a body of persons who are in close business relationships and who perform large-scale transactions in relation to any commodity³.

The market economy means even interdependence between *four markets*: the goods and services market, the labour market, the information market and *the financial market*.

The one who presents interest for the current analysis is the latter, as the market where the financial assets are traded.

The financial assets are the valuable documents that consecrate current or future financial entitlements of their holder, resulting from their capitalization (interest, dividends, etc.). They differ from real assets which are tangible or non-tangible goods which generate income in the future in the form of monthly rent, rents, profits, but are the money correspondent of the real assets, thus revealing the dual nature of the market economy, consisting of a real economy (the material processes of producing the goods and the services necessary for the individual consumption and the resume of the production) and the symbolic or financial economy (informational type processes, represented by the movement of the money and securities)⁴. The financial asset may be: the exchange value, when the good (viewed as commodity) helps to obtain another good; the investment value (capital) when the good is used to produce revenue in the future.

The financial assets may be: banking assets; non-banking financial assets; capital assets; monetary assets. To this, the hybrid assets (deposit certificates, etc.) are added.

*The financial market is composed of three components, depending precisely on the type of financial assets that are traded within it*⁵:

1. the banking market - is characterized by transactions with banking assets resulting from banking operations carrying a high level of safety interest.

2. the money market - through it, monetary transactions are made between the residents of a country, using the national currency.
3. the capital market - specialized in the intermediation of transactions with financial assets that have maturities on average terms (1 to 5 years) and long terms (over 5 years). Through this market, the applicants' capital needs are met by the bidders' capital availability.

The capital market exerts the following functions:

1. issuance and sale for the first time of the financial titles of the issuers or the debtors toward the owners of financial capital who wish to buy financial assets;
2. negotiation of securities, provided that they are sold and converted into liquidities by their first holders and prior to maturity.

The components of the capital market⁶ are: the primary market (where the first placement of the securities issue takes place) and the secondary market (where the securities absorbed by the primary market are bought by banks, investors and private individuals).

Article 1 paragraph (1) of the Law no. 297/2004, on the capital market, regulates the establishment and the functioning of the financial instruments markets, with their specific institutions and operations, as well as the collective investment bodies in order to mobilize the financial resources through investment in financial instruments.

2. The offense foreseen in article 279 letter b) and article 245 of the Law no. 297/2004 - the use without right of the privileged information (inside trading)

In accordance with the legal texts previously quoted: "The violation of the provisions of article 245 paragraph (1) constitutes a crime and is punished by imprisonment from 6 months to 5 years and the interdiction of some rights: It is forbidden for any person possessing privileged information to use that information for the acquisition or disposal or for the intention to acquire or dispose of, for himself or for the account of a third party, directly or indirectly, of the financial instruments to which such information relate to".

Along with other texts of incrimination, the Law no. 297/2004 also includes the one quoted above. The offense so described is thus committed by an act of use for own account of privileged information by the person who knows the information, that results in the acquisition or disposal of financial instruments to which that information relates.

The legal specific object of the offense is to protect the capital market against unfair activities. It is

³ V. Stoica, E. Ionescu, Capital Markets and Stock Exchanges, 2nd edition, Economica Publishing House, Bucharest, 2002, page 14.

⁴ I. Popa, The stock-exchange, 2nd edition, volume I, Adevarul Publishing House, Bucharest, 1995, page 28.

⁵ V. Stoica, E. Ionescu, Op.cit., page 16.

⁶ O. Stoica, Mechanisms and institutions of the capital market, Economica Publishing House, Bucharest, 2002, page 20.

important to ensure that this value is respected as market mechanisms will not function properly and the chances of those involved in trading activities are not equal.

We consider that the crime has no *material object*, since the use to which the incriminating rule refers to consists concretely in trading or the intention to trade securities on the capital market and this activity does not affect the information, but the market share of the securities.

The active subject of the offence is a qualified one. Anyone with privileged information may be in this position:

- a) in his capacity as a member of the board of directors or of the managerial or supervisory structures of the issuer;
- b) as a result of its holdings in the issuer's share capital;
- c) by exercising his / her function, profession or duties;
- d) illegally or fraudulently, as a result of criminal activities.

Moreover, the article 247 of the Law no. 297/2004 broadens the scope of the active subjects of the crime we are studying and of the one that follows. This text specifies that the provisions of the article 245 and the article 246 shall apply to any other person who holds privileged information, provided that those persons know or should have been aware that that information is privileged.

Another category of persons who may become active subjects of crimes is the one consisting of persons responsible for executing orders related to trading financial instruments when the information relates to the orders given by clients and not yet executed.

The passive subject is the State, as the holder of the obligation to ensure, through C.N.V.M., the legally functioning of the activity in the capital market field. There may be a natural or legal person injured by the market abuse, as a secondary subordinate subject.

The material element consists in a commissive behaviour to use the privileged information under conditions other than those lawfully admitted. In this way, the crime is to use in the unauthorized ways indicated by the incriminating norm of the privileged information, which due to its specificity can lead to abuse of the capital market. In concrete terms, it will be about the use of such information for the acquisition or disposal of or for the intention to acquire or dispose of, on its own account or on the account of a third person, directly or indirectly, of the financial instruments to which this information relates to.

In order to achieve the objective content of the offense, however, we appreciate the need to meet the following *essential requirements*:

- a) *there is an activity of using the privileged information*. The use may take the form of securities trading activities on the capital market (e.g. - an information is known about

the imminence of the state of insolvency of the patrimony of a company whose shares are held by the person who has access to this information. The shares are immediately sold at the usual trading price and financial loss caused by the disclosure of the information is avoided).

In the legal interpretation provided by the article 244 of the Law no. 297/2004, *privileged information* means the information of a precise nature which has not been made public and which relates directly or indirectly to one or more issuers or to one or more financial instruments and which, if publicly disclosed, could have a significant impact on the price of those financial instruments, or on the price of related derivative instruments.

When referring to commodity derivatives, "the privileged information" shall mean the information of a precise nature which has not been made public and which relates directly or indirectly to financial derivatives and which the participants in the markets on which those financial derivatives instruments are traded are expected to receive it, in accordance with the accepted market practices.

For the persons in charge with the execution of orders for the trading of financial instruments, "the privileged information" means as well the accurate information sent by a client about his orders that have not yet been executed, relating directly or indirectly to one or more issuers or to one or more financial instruments, information which, if made public, could have significant effects on the price of those financial instruments or on the price of the derivative financial instruments with which they are related.

- b) *the activity must be performed by the person who knows such information*. The requirement concerns the circumstance in which, when the use is made by another person, even at the instigation of the person who knows the privileged information, the act committed will be the one provided for in article 279 letter b) and article 246 of the Law no. 297/2004.
- c) the third essential requirement is that it *is mandatory for transactions not to be made*, considering that the person engaged in such transactions had a contractual obligation to acquire or dispose of financial instruments and that this contract was concluded before the respective person had the privileged information. If the requirement is not met, we will be faced with a cause of special justification.

According to article 12 of the Law no. 78/2000 on the prevention and sanctioning of the corruption, the following actions shall be punished by imprisonment from one to five years, if they are committed for the purpose of obtaining for themselves or for another money, goods or other undue advantage: a) performing financial operations, as acts of commerce incompatible with the function, the duty or the assignment of a person

or the conclusion of financial transactions, using the information obtained by virtue of his or her function, duty or assignment; b) the use in any way, directly or indirectly, of information that is not intended to be advertised or to allow unauthorized persons to have access to such information.

On the other hand, by article 245 of the Law no. 279/2004 any person possessing privileged information is forbidden to use that information for the acquisition or the disposal or in order to acquire or dispose, on his own account or on behalf of a third party, directly or indirectly, of financial instruments to which that information relates.

By comparing the two legal texts, it can be easily observed that the difference between them is due to the existence of an additional condition in article 12 of the Law no. 78/2000⁷. Apparently, the two criminal norms [article 279 of the Law no. 297/2004 and article 12 letter b) of the Law no. 78/2000] are identical, refer to the same situations and are therefore concurrent. This simple analysis, however, does not resist when performing a legal, literary, rational and systematic interpretation, with the observance of the strict interpretation of criminal laws, but without extending them.

Thus, the offense under the law regulating the capital market refers to “own advantage or the advantage of third parties”, a much narrower concept in its content than the wording of the Law no. 78/2000 – “for the purpose of obtaining for himself or for another money, goods or other undue benefits”. In the first case, we face a hypothesis of a facility in relation to the other participants in the capital market operations, being an unfair speculation. The condition regarding the purpose within the regulation of article 12 of the Law no. 78/2000 largely exceeds the previous case, as it implies a very elaborate volitional process that seeks to obtain undue use of a certain benefit, asset or money, that is not legally due and cannot be procured otherwise than in violation of the law⁸.

Thus, the action of any *person holding privileged information insider* who purchases or sells for himself or for another, directly or indirectly, movable assets or other rights related thereto of the issuer in respect of which he holds the respective privileged information, or makes use of the information in any other way and transmits them or facilitates their publication for the benefit of themselves or of third parties, is sanctioned under the law of the capital market.

The *immediate consequence* of the offense is to jeopardize the proper conduct of the business in the capital market. The causality link results from committing the material element.

The *form of guilt* with which the offense is committed is the intention. We appreciate that each time the mode of intent will be the direct one.

Given the provisions of article 16 paragraph (6) Criminal Code, we appreciate that the intention is the form of guilt with which is committed the offense provided for in article 279 letter b), article 245 of the Law no. 297/2004 and in the hypothesis regulated by article 247 of the Law no. 297/2004 which considers the situation of committing the offense by another person who has acquired the privileged information. It is noted that engaging in a trading activity on the capital market before the information is made public makes the content of the offense only if those individuals know or ought to have known that that information is privileged. This last formula, “ought to have known” is characteristic from the intelligible point of view of the guilt without provision. However, if there is no mention of committing the act with guilt, it follows the common rules, being mandatory to be committed with intent. In fact, it can happen that the person learns about the privileged information before being advertised and that the person performs a trading activity, being in fault regarding the specific nature of the information he uses in this way. There is thus a contradiction between the indication of the intentional nature of the non-compliance with the obligations imposed by the law and the specific attitude of the form of fault. However, we interpret the text in the sense that the act will always be committed with direct intent, the information being used with the clear representation of its privileged character.

The motive and the purpose are elements of individualisation of the punishment.

The offense is with intent (wilful) and, for this reason, it may also know atypical modes of the acts of preparation and attempt. Neither the former nor the latter are sanctioned by the criminal law.

The primary *punishments* that may be applied for committing this crime are imprisonment from 6 months to 5 years and the interdiction of certain rights.

Where the privileged information is used by a legal person, the interdiction shall also apply to the natural person who took part in the decision to execute the transaction on the account of that legal person.

3. Conclusions

The capital market is of great importance, and because of its specificity it is difficult, if not impossible, to be protected to an effective extent by the risk of having within it antisocial behaviours being committed whose gravity would justify the intervention of the criminal law. By the completion norms it provides, but also by the incriminating rules it regulates, the Law no. 297/2004 has taken on the difficult role to prevent and combat, at least at the virtual level, the criminal deeds that could be committed in this context and which could disturb it in a serious way.

⁷ D. Ciuncan, Corruption Offenses. Regulations apparently parallel, R.D.P. no. 3/2005, p.78.

⁸ See P. Narița, Criminal investigation in causes that are in the jurisdiction of the National Anti-Corruption Prosecutor's Office regarding offenses within the market of financial instruments (capital market), Documentary Bulletin no. 3/2004 of P.N.A. / D.N.A. (<http://www.pna.ro>).

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