

Regulatory Investigations Group

Ian Charles Hannam v The Financial Conduct Authority Inside information clarified?

In its decision in *Ian Charles Hannam v The Financial Conduct Authority*¹, the Upper Tribunal (the "Tribunal") provided some highly anticipated and much needed clarification on the definition, and treatment, of inside information. Reflecting the complexity and importance of the case, the 130 page judgment will undoubtedly have repercussions throughout the financial services sector and serve as a precedent for future cases involving allegations of improper disclosure of inside information.

We have set out below a summary of the key findings in relation to the meaning of inside information and some practical steps to take in response to the case.

Background

In a Decision Notice dated 27 February 2012, the FSA, now FCA², fined Mr Hannam, a senior banker at J.P. Morgan, £450,000 for improperly disclosing inside information contrary to s118(3) of the Financial Services and Markets Act ("FSMA") in two emails sent on 9 September 2008 and 8 October 2008 respectively.

Improper disclosure is conduct where an insider discloses inside information to another person otherwise than in the proper course of the exercise of his employment, profession or duties.

Mr Hannam referred the matter to the Upper Tribunal.

The Tribunal's decision

The Tribunal found that the emails contained inside information for the purposes of FSMA, and that the inside information was not disclosed in the proper course of Mr Hannam's employment.

What is inside information?

For information to be "inside information" it must, amongst other things,

- be of a **precise nature**; and
- be information that would, if generally available, **be likely to have a significant effect on the price** of the qualifying investments or on the price of related investments.

Precise

Information is "precise" for these purposes if it (a) **indicates circumstances** that exist or may reasonably be expected to come into existence or an event that has occurred or may reasonably be expected to occur; and (b) is specific enough to enable a conclusion to be drawn as to **the possible effect** of those circumstances or that event **on the price** of qualifying investments or related investments.

The Tribunal considered that the question of whether information was precise gave rise to a number of issues:

- (1) **The extent to which information must be accurate in order to be sufficiently precise to constitute inside information.** The Tribunal concluded that information which is not wholly accurate may, nonetheless, convey a message to the recipient which may give the recipient an advantage over other market participants and is therefore capable of amounting to inside information notwithstanding its inaccuracy.
- (2) **The meaning of "possible effect"**, in the context of the requirement that information should be specific enough to enable a conclusion to be drawn as to the possible effect on price. The Tribunal found that it was necessary for the information to indicate the direction of movement but not the extent to which the price might be affected. The information does not have to be such as to enable an investor to know *with confidence* that the price *will* move if the information were made public.

Likely to have a significant effect on price

- (1) **The interaction between the "price" and "reasonable investor" tests.** S118C(2)(c) FSMA requires that the information in question would, if generally available, be *likely to have a significant effect on the price* of the relevant securities and s118C(6) provides that information would be likely to have a significant effect on price if and only if it is information of a kind which a reasonable investor would be likely to use as part of the basis of his investment decisions. The Tribunal considered the reasonable investor test in s118C(6) to provide the definition of what would be likely to have a significant effect on price

¹ [2014] UKUT 0233 (TCC)

² For convenience, reference is made to the "FSA" throughout this note.

for the purposes of s118C(2)(c), but that the definition must be applied in the context of the price test. In particular, it said that *"the reasonable investor is an investor who would take into account information which would be likely to have a significant effect on price. Conversely, he is an investor who would not take into account information which would have no effect on price at all . . ."*. This contrasts with previous decisions where it had been found that no expected price effect was required.

- (2) **The meaning of significant.** The Tribunal found that "significant" for these purposes was only to be contrasted with insignificant, in the sense of trivial.
- (3) As to **the meaning of "likely"**, the Tribunal found that information which was "likely" to have a significant effect on price was information where there was a real (and not fanciful or *de minimis*) prospect of the information having an effect on the price of qualifying investments. It does not need to be more likely than not.

Other issues

The Tribunal addressed some additional issues of interest, including:

- that information can be improperly disclosed to an individual even if the recipient is already in possession of it; and
- reaffirming that there is no difference in the concept of inside information when used in the context of an issuer's obligations to disclose inside information promptly and publicly (unless a specific exemption applies) and when used in the context of the improper disclosure and insider dealing offences.

Disclosure in the proper course of employment

The Tribunal considered whether, if the emails did constitute inside information, Mr Hannam had disclosed them in the proper course of his employment. Mr Hannam argued that the disclosures were made in the proper course of his employment given that both of the emails were sent: (i) in furtherance of Mr Hannam's mandate to facilitate a corporate transaction, (ii) with the implicit authority of his client, and (iii) on the understanding that the information was being received in confidence and would not be abused. However, the Tribunal disagreed.

Amongst other matters, the Tribunal found that:

- whilst the emails were sent in the course of Mr Hannam's employment, this did not mean that this was necessarily in the "proper" exercise of his employment; and
- it would never be in the proper course of a person's employment for him to disclose inside information to a third party where he knows that his employer and client would not consent to the public disclosure of that information.

The Tribunal found that the information disclosed in both of the emails could only be disclosed if the recipient was under an obligation of confidentiality, which was not satisfied in the present case. A mere understanding on the part of the recipient of the need to keep information confidential (had it existed) was insufficient to impose a confidentiality obligation.

Important practical steps

The case covers some important issues which need to be reflected in practice. Firms should therefore be considering a number of steps, including:

- updating their personnel in relation to the key messages to emerge from the case, whether in the form of training or a written update;
- engaging specifically with the teams who broker transactions to ensure that they understand the need to avoid communicating insider information (and also to avoid misleading communications). A mechanism for approving communications might be considered;
- reinforcing the need to impose confidentiality obligations before communicating inside information (as opposed, say, to relying on a hoped-for understanding that the circumstances demand confidentiality). This should be reflected in the procedures used for making an individual an insider;
- putting in place additional safeguards in potential bid scenarios since emphasis was placed on the need to comply with the Takeover Code;
- updating teams who advise issuer clients, given that the case underlined the parallel with the obligations of issuers to disclose inside information.

For further information on any of the issues discussed above, please contact any of the regulatory investigations partners named below.

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