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Financial Services and Markets

Market Abuse - The Greenlight/Einhorn Case

On 25 January 2012, the FSA published findings of market abuse, and aggregate fines of £7.2 million, against U.S. hedge fund manager Greenlight Capital, Inc. and David Einhorn, its sole portfolio manager.

The case related to a conversation held between Mr Einhorn and representatives of Punch Taverns Plc ("Punch") and its broker prior to a significant new issue of shares by Punch. Mr Einhorn had requested that the call proceed on a "non-wall crossed" basis, but the FSA found that he had nonetheless received inside information. Greenlight dealt in Punch on Mr Einhorn's instruction shortly after the call.

The FSA found that both Mr Einhorn and Greenlight Capital (to which Mr Einhorn's behaviour was attributable) had engaged in market abuse. The FSA commented that:

> "*Given Mr Einhorn's position and experience, it should have been apparent to him that the information he received on the Punch call was confidential and price sensitive information that gave rise to legal and regulatory risk. The Punch call was unusual in that it was a discussion with management following a refusal to be wall crossed. In the circumstances Mr Einhorn should have been especially vigilant in assessing the information he received*."

Key points

- It is not sufficient, having indicated a desire not to be provided with inside information, to assume that no such information has been provided. Reliance cannot be placed on the fact that a dialogue has been expressed in conceptual or hypothetical terms if, in fact, inside information is imparted.
- The case underlines the territorial reach of the market abuse regime and its application to those doing business outside the UK and the rest of Europe. Mr Einhorn and Greenlight Capital, Inc. were in the United States. Interestingly, Mr Einhorn is reported as commenting that the case will change the way in which he deals with UK companies. The scope of the regime is much broader than that and applies to all securities (and their derivatives) which are tradeable on European regulated markets. It is not necessary for securities to be European or to have a European listing in order to be admitted to trading on European markets. This was a key point in the 2006 case against GLG Partners and Philippe Jabre which related to Japanese securities listed in Tokyo but tradeable on the London Stock Exchange's International Bulletin Board.
- A number of the findings were consistent with previous cases and/or guidance in relation to the meaning of "inside information" but nonetheless serve as reminders. These include that:
    - it was not necessary for it to be certain that the equity issuance would occur in order for the information imparted to constitute inside information: a reasonable expectation was sufficient;
    - one test of inside information is that the information is specific enough to enable a conclusion to be drawn as to its possible effect on price: in this context a conclusion about the likely direction of movement is sufficient (it is not necessary to be able to assess likely quantum of movement).
- The FSA maintained its controversial stance that the requirement that information, if disclosed, would have a "significant effect on price" means information that, if disclosed, a reasonable investor would be likely to use as part of the basis of his investment decisions (irrespective of whether the price would move). This stance is contrary to CESR guidance. In this case the distinction may have been academic.

Key messages

The important practical reminders from the case are as follows:

- Mr Einhorn made it clear at the start of the conversation that he did not wish to receive inside information. This remains best practice. The findings and sanctions may have been considerably worse had Mr Einhorn not done so.

- A statement that the recipient of information does not wish to receive inside information is not, however, complete protection. It remains the responsibility of every person receiving information in whatever form to assess at the end of the conversation, or series of conversations, whether inside information has been imparted. While assurances from the issuer or its broker may be helpful, they are not conclusive. Pieces of information should be looked at both individually and in aggregate. Particular attention should be paid to impressions which can be formed even where the words themselves are expressed in conceptual or hypothetical terms.

The case also serves as a reminder of the fact that the FSA will not be deterred from pursuing those who they perceive to be wrongdoers even if based overseas.

The decision notice is silent as to whether culpability should be shared with Punch's broker. It remains to be seen whether more will emerge.

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