

# Towards harmonization of insider trading criminal law at EU level?

Pr Michael Faure,  
*Maastricht University, METRO*

Dr Claire Leger,  
*Université Paris Ouest Nanterre la Défense*  
*OECD Anticorruption Division*

EFFACE Workshop, September 2015, La Haye

# Scientific and societal relevance

- Insider trading prohibition in Europe : around 1990
- Recent financial crisis : increasing demand for financial regulation
- Internationalisation of the world's securities market : challenges traditional notions of regulation and enforcement

- ***Evolution of EU criminal law***

1999: the Maastricht Treaty: PJCC

2005: European Court of Justice Environmental Crime Judgment

2008: Environmental Crimes Directive

2009: Directive on Ship Source Pollution

2009: the Lisbon Treaty: Article 83(1) / **Article 83(2) TFEU**

- ***Evolution of EU insider trading law***

1989: Insider Dealing Directive

2003: Market Abuse Directive

3rd of July 2014: The Directive 2014/57/EU on Criminal Sanctions for Market Abuse: First to be based on the **article 83(2) TFEU**

# Research questions

- 1) Is under all circumstances criminal law necessary to enforce insider trading laws?
- 2) Even if criminal law is prescribed in certain circumstances, should it be introduced at EU level?

# Goal of the research and methodology

- Law and economics theoretical approach to the criminalization of insider trading at EU level
- Critical analysis of the Directive 2014/57/EU on criminal sanctions for market abuse

# 1/ Is criminal law necessary to enforce insider trading laws?

- *Deterrence theory*
- *Public vs Private enforcement of laws:*
  - Need for stringent sanctions in case of:  
Low probability of detection  
High social harm  
High gain
  - Low incentive to enforce the law by private party  
(insufficient financial gain, rational apathy, dispersed ownership, private interest, public harm)

- ***There is a need for the most stringent sanctions through criminal law in case of :***
  - Very low probability of detection and apprehension,
  - Very high and substantial gain,
  - Very high social harm: large, immaterial, diffuse.
  
- ***Qualities of criminal law that makes it a unique tool to achieve deterrence and incapacitation:***
  - Exclusive availability of social incapacitation: needed to achieve deterrence (limited wealth) or incapacitation (violence or undeterrable offenders),
  - Inherent stigma reinforces the deterrence effect,
  - High procedural requirements: reduction of error cost.

- ***Insider trading dangerousness for society***

Not violent offenders, mostly first time offenders (67,5%).

- ***Insider trading gain***

Median of \$25,594, Mean of \$215,696.

- ***Insider trading harm***

Insider trading harms fairness and justice,

Harm measurement is controversial from an economic perspective.

- ***Insider trading's probability of detection***

Immaterial and diffuse nature,

International, anonymous trade based on legitimately acquired confidential information resulting from position,

Insiders hide their trade, use proxies or intermediaries.

- ***Insider trading's probability of conviction***

Difficulty to establish:

- the materiality,
- the non-public quality of the information,
- guilt.

## ***Conclusion***

Criminal law is necessary to optimally deter insider trading.

## 2/ Should criminal insider trading law be introduced at EU level?

Criminal insider trading law regimes of the Member States show divergences in:

- types,
- levels of sanctions,
- procedures (cooperation and cumulation of sanctions),
- resources allocated to enforcement (staff and budget),
- enforcement of insider trading laws.

***The Directive on criminal sanctions for market abuse***, (article 83(2) TFEU) requires Member States:

- To take the necessary measures to ensure that insider dealing constitutes a criminal offence (not the case in one country: Bulgaria)...
- ...When committed intentionally (Art.3) (not the case in 10 Member States: Cyprus, Germany, Denmark, Spain, Finland, Latvia, Malta, Netherlands, Sweden, United Kingdom),
- ...To ensure that insider trading is punishable by a maximum term of imprisonment of at least four years (Art.7) (not the case in 7 Member States: Belgium, France, Lithuania, Luxembourg, The Netherlands, Estonia, Hungary),
- ...To ensure that legal persons can be held liable for criminal insider trading (Art. 8) (not the case in 8 Member States: Bulgaria, Czech Republic, Germany, Greece, Luxembourg, Poland, Portugal, Sweden).

## ***Economics of federalization approach : Normative legal standard setting VS method of enforcement setting***

- ***Inter-jurisdictional externalities***

Despite internationalization of the securities market insider trading problems are not always transboundary and cooperation may be sufficient to address them.

- ***Jurisdictional competition***

Law being a product, competition amongst suppliers may result in a better satisfaction of consumer preferences : “Race to the top”.

- ***Transaction costs***

Transaction costs savings are likely to be relatively small and substantial benefits can be gained from preference for differentiation : learning effects.

## ***Commission legal perspective***

- ***Compliance with legal basis Art.83(2) TFEU?***

- **Guidelines** : COM(2011) 573 final “Towards an EU Criminal Policy: Ensuring the effective implementation of EU policies through criminal law”: art. 83(2) calls for clear reliance on empirical data regarding the essential need of introducing criminal sanctions at EU level

- **Commission’s motivation and arguments** of abstract and symbolic nature : based on conferences and consultations,

No empirical evidence of ineffective enforcement at MS level or that criminalization at EU level would remedy those supposed problems.

## ***Consistency of the Directive with the fundamental principles of criminal law?***

- *Ultima ratio* principle
- Principle of subsidiarity
- Principle of coherence
- Principle of guilt

## ***Conclusions***

- Economic theory casts doubt on whether there is effectively a need of imposing criminal sanctions at European level,
- Arguments of the Commission to criminalize insider trading at European level are not convincing,
- The contents of the Directive is to a large extent inconsistent with fundamental principles of criminal law,
  
- The European Commission should first improve the functioning of private or administrative enforcement of insider trading laws at a EU level.

Thank you for your attention