

“Russia Enacts Its First Rules on Insider Trade”

Ilya Goryachev, Lidings Associate

On 29 July 2010, President Medvedev, signed the law «On measures against unlawful dissemination of insider information and market manipulation and on amendments to some laws of the Russian Federation” (the Law). The Law strikes as one of the confidence-building measures among investors in the Russian economy. Another aim is to improve the process of market trade. The Law is of particular interest for foreign investors and other players in the financial market.

One of its goals is to eliminate manipulations in securities and credit markets, in investment banks and investment funds transactions. This goal is especially relevant for creating a favorable investment climate on Russia. Let’s have a closer look at the Law

Among other things, it specifies:

- definitions of insider information and market manipulation;
- express prohibition on disclosure of insider information to third parties including its usage in transactions involving financial instruments, securities and goods;
- types of individuals and legal entities classed as insiders as well as their obligations resulting thereof;
- new powers of the Federal Financial Markets Service (hereinafter- the FFMS) with regards to insider information;
- liability of both individuals and legal entities for violations of the insider information regime.

The Law is to enter into force on 27 January 2011 (180 days after its publication). However we can already examine its key provisions.

I. Insider information regime

Insider information is defined as precise and profile information (including commercial, official, bank, state, tax, postal and other secrets protected by law), dissemination of which may have a substantial impact on the price of:

- financial instruments;
- foreign currency;
- goods.

As an example of insider information or, to be more precise, of negative impact of its usage, one can look at a typical situation in the securities market when an insider disseminates false information about an issuer thus influencing sales of its securities at an overestimated or underestimated price. As a result of this, ordinary investors turn out to be at a loss. Or for instance, an illustration of “state inside”, was when statements made by public officials concerning the Yukos case caused upward and downward fluctuations of the company shares.

However, it should be pointed out that the following is not considered as insider information:

- information, that turned out to be public as a result of (including but not limited to) its dissemination;
- researches, prognoses and calculations concerning financial instruments, foreign currency and goods, that were based on available public information, including recommendations and suggestions concerning operations with regards to financial instruments, foreign currency and goods.

II. Individuals and legal entities classed as insiders

The Law labels 13 types of insiders, which can be split into 5 main groups:

- Market Participants: issuers, management companies, professional securities market participants, other persons that effect transactions on behalf of their clients, trade organizers, clearing organizations and also depositaries and credit institutions;
- Corporate Entities: economic operators that occupy a dominant position in the particular market, individuals that have access to insider information on the ground of agreements (including auditors and appraisers), members

of the Board of Directors and the General Shareholders Meeting;

- Individuals that have access to insider information under civil and labor law contracts;
- Public Law Actors: government authorities, their heads, municipal authorities and their heads, Bank of Russia, members of the National Banking Board;
- Media and Rating agencies.

III. Obligations of insiders

Legal entities occupying a dominant position in a market and issuers are obliged to keep an insiders record. Moreover, legal entities have to inform insiders of them being included in such listing. The Law also provides for submission of the record to trade organizers and the FFMS. But this is not the whole story: legal entities specified in the Law are to appoint a public officer or to establish a department in charge of exercising control over the insider information regime. The point is that the insider information regime varies from company to company as it shall be determined in accordance with a company's internal documents on insider information and access to it. The Law will be of particular interest to trade process organizers and management companies as their insiders are obliged to inform them and the FFMS of concluded transactions.

IV. New powers of the FFMS

Under the Law the FFMS may carry out inspections to protect the insider information regime. The only condition for such an inspection is a complaint of dissemination or a publication in mass media. The state authority may also order to eliminate violations of the insider information regime. Moreover, the FFMS is entitled to address licensing bodies regarding a license withdrawal.

It is important to point out that the FFMS can demand submitting of the data exchange record for the purpose of preventing violations. It is the FFMS that will issue subordinate legislation on the exercise of the powers listed above. Insiders shall pay particular attention to it.

V. Liability for violations of the insider information regime

The Law introduced amendments to the Criminal Code (unlawful intentional usage of insider information will be punished by a fine of 300 000 – 500 000 roubles or by imprisonment for 2-4 years) and to the Code of Administrative Offences (unlawful usage of insider information when it doesn't result in large-scale damages will be punished by a fine of 3 000 – 5 000 roubles for individuals; 30 000 - 50 000 roubles for officials and not less than minimum 700 000 roubles for legal entities depending on the excessive income. Brokers and dealers that committed violations will undergo a risk of license annulment. In order to recover the damages, caused by the unlawful usage of insider information, it is possible to file a civil action against the insider at issue. However, the mere fact that the operations were conducted using insider information, will not be considered as the ground for their nullity.

VI. Preliminary conclusions

Generally speaking, the Law can be characterized as a positive sign, as in the absence of such a law it would be somehow difficult to protect prospective investors. However, some experts believe that the Law will lead to appearance of other intricate insider schemes to escape liability. Anyway, depending on the future enforcement practice of this Law we will be able to decide whether it is effective or not.

The comment has been prepared by Ilya Goryachev, Lidings Law Firm Associate. If any questions occur you can contact him: IGoryachev@lidings.com, Phone: +7 495 989-44-10; Fax: +7 495 989-44-20