INSIDER TRADING: HOW TO CONTROL AND REGULATE

Abstract: The article is devoted to the problem of insider trading and its regulation in modern law systems. The author gives a definition of the term. The regulation of the insider trading in Russia and the USA are considered. The importance of such documents as Securities and Exchange Act, Market Abuse Directive, Federal Law No 224 «On Insider Trading and Market Manipulation» is highlighted. The author comes to the conclusion that the government should establish and develop the common ground for solving the problems related to insider trading.

Key words: insider trading, regulation, Securities and Exchange Act, Market Abuse Directive, Federal Law.
Nowadays insider trading is one of the widely discussed topics in the field of trading securities on the secondary market. Insider trading, as a phenomenon, originates from the market efficiency hypothesis, which was introduced by the professor Eugene Fama in the 1970s [3]. The theory states, that all available information on the market is already integrated into the price of all stocks traded on the market, which follows all of the criteria of efficiency. Apparently, that means all efforts, undertaken to beat the market using «additional» information, possessed by the investor, are in vain. That happens, because the market responds immediately to all possible information and adjusts the prices in respect to that, so the «additional information», the investor allegedly possesses and tries to use in order to beat the market and earn the abnormal return, was already included in the price of the stock.

Due to the theory, developed by Eugene Fama, there are different levels of market efficiency: weak form, semi-strong form and strong form [2].

The last and the most prominent form is a strong form of efficiency. This implies that the market prices are even adjusted to the private information, held by several players on the market or even by people, who don’t have any relation to it.

Using of confidential information undermines the rules of fair trade and consistency of the market. Insider trading is considered to be illegal activity and prohibited under different sets of regulations. What are the basics of International Regulation?
The basic act for insider trading regulation in the USA is Securities and Exchange Act of 1934 [3]. The SEA authorized the formation of the Securities Exchange Commission (SEC), which oversees investors and companies all over the world. Every country has a number of regulatory or supervisory institutions (usually governmental or administrative bodies), which are aimed at collecting information, concerning suspicious transactions; identifying the parties to suspicious transactions; analyzing the previous activities of identified investors and triggering the insider trading. Insider trade regulation is also regulated by the means of Market Abuse Directive (MAD), which requires Member States to enforce criminal penalties and sanctions on the criminal offences as described in the Directive.

A problem of insider trading in the Russian Federation has been widely discussed in financial circles since mid-nineties, but the law was introduced only in July 2010 (Federal Law No 224 «On Insider Trading and Market Manipulation») [1]. Since that times, the law hasn’t been seriously amended (the latest amendment dated 2013). It means that the same rules on insider trading have been used for 4 years. Therefore, there is a need of authorities to pay attention to this problem.

Thus, investigating this issue I have come to the following conclusions:

- the insider trading is an unfair use of confidential information in order to gain abnormal returns in trading process. Law provisions, considering the insider trading are used in every country with financial markets regulation. Every system has its own distinctive features and every system is dynamic, i.e. subjective to the new cases and changes in financial markets
- it is hard to detect the insider trading and prove the facts of trading, using the inside. It is even more challenging to accuse someone on these grounds and find sufficient evidence for that. However, there exists a need of these
regulations: this way the companies could protect themselves against the financial turbulence. Such organizations as SEC nowadays widely investigate the insider trading cases and gather information on such cases in order to establish and develop the common ground for solving such kind of problems.

References