AN ANALYSIS OF THE GENERAL ENFORCEMENT APPROACHES TO COMBAT MARKET ABUSE (PART 1)*

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SUMMARY

This article analyses the role and use of selected general anti-market abuse approaches in order to increase awareness and enforcement on the part of the relevant stakeholders. To this end, the article provides an evaluation of selected general anti-market abuse-enforcement approaches as well as the significant advantages and disadvantages of such approaches. This is done in two parts: firstly, Part I discusses the anti-market abuse measures that primarily deal with enforcement and Part II discusses anti-market abuse measures that primarily deal with surveillance, detection and investigation which will be covered in the next article.

1 INTRODUCTION

It is generally accepted that there is no comprehensive and satisfactory definition of market abuse that exists to date.¹ However, for the purposes of this article “market abuse” is used as a generic term referring to insider

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trading and market manipulation. Effective enforcement plays a vital role in the successful implementation of any legislation. South Africa has market-abuse legislation in place but nonetheless there are no specific regulations and/or sufficient relevant information on the measures or general approaches that are employed to enhance the implementation of such legislation to combat market abuse. The objective of this article is to analyse the role and use of some selected general approaches to combat market abuse in order to increase awareness and enforcement on the part of the relevant stakeholders globally. To this end, this article provides an evaluation of selected general anti-market abuse-enforcement approaches and the significant advantages and disadvantages of such approaches. This is done in two parts: firstly, this article discusses the anti-market abuse measures that primarily deal with enforcement and secondly, the discussion on anti-market abuse measures that primarily deal with surveillance, detection and investigation which will be covered in the next article.

2 ANALYSIS OF ANTI-MARKET ABUSE MEASURES THAT PRIMARILY DEAL WITH ENFORCEMENT

2.1 The role and use of criminal measures to combat market abuse

Market-abuse practices are outlawed and treated as criminal offences in a number of countries globally. Put differently, criminal measures such as monetary penalties (fines) and imprisonment of the culprits involved are employed to combat insider trading, market manipulation and other related market-abuse activities in many jurisdictions.

For instance see generally Janks and Serchuk “Administrative Penalties: A Deterrent to Market Abuse?” (2009) 1-3 http://www.bowman.co.za/LawArticles/Law-Article~id~2132417421.asp (accessed 2009-08-12), who argues that the introduction of administrative penalties for market abuse in South Africa has now, to a greater extent, provided a more deterrent effect on the part of the market-abuse offenders; and Berkahn Regulatory and Enabling Approaches to Corporate Law Enforcement: Patterns of Litigation 1986-2002 and The Effect of Recent Reforms in New Zealand, Australia and the United Kingdom (2006) 10-18, for a discussion on the merits and demerits of public and private enforcement of securities laws. It should be noted that the discussion does not exclusively focus on the anti-market abuse-enforcement approaches that are employed in a particular specific jurisdiction alone. The focus will be on the anti-market abuse-enforcement approaches that are commonly employed in different jurisdictions. Where necessary, consideration will also be given to pertinent theoretical arguments regarding the enforcement approaches that may have been used to curb market abuse more successfully than others in such jurisdictions.


It is submitted that Moohr argues correctly that the use of criminal measures has to date played an important role to create internalized norms for market-abuse deterrence among the relevant stakeholders in several countries. Another advantage of using criminal measures to prohibit market abuse is that such measures are commonly enforced publicly through the relevant government departments and the courts, thus eliminating potential problems of overdeterrence and lack of resources on the part of some independent regulators. Additionally, Lynch argues insightfully that criminal measures play a big role in combating market abuse and in “bolstering moral incentives” through the reinforcement of society’s moral standards and stigmatizing those who violate them. In other words, Lynch submits that the use of criminal measures promotes good moral activity among all the market participants, which in a way has a positive deterrent and retributory effect against market-abuse offenders.

Criminal measures are not without shortcomings. Avgouleas contends that the burden of proof beyond a reasonable doubt, required in criminal cases of market abuse, is seriously difficult to achieve for the prosecuting authorities in many countries. This has affected the successful prosecution of market abuse cases negatively in some jurisdictions, inter alia China, Australia, South Africa and United Kingdom. In the same vein,

6 Moohr 2003 Florida LR 949-951.
7 Coffee “Law and the Market: The Impact of Enforcement” 2007 University of Pennsylvania LR 230 302-308, who submits that the United States of America’s private enforcement of securities and market-abuse laws seldom impose penalties on the culpable offenders, hence more emphasis should now be placed on public (government and courts related measures) enforcement of such laws; Russen Financial Services Authorisation, Supervision, and Enforcement: A Litigator’s Guide (2006) 177-179; and Lyon and Du Plessis The Law of Insider Trading in Australia (2005) 114-117, for further analysis of the criminal measures that are used to prevent securities law violations like market abuse in the United Kingdom and Australia respectively.
14 See further Barnes “Insider Dealing and Market Abuse: The UK’s Record on Enforcement” 2010 1-19 http://mpra.ub.uni-muenchen.de/25585/1/insiderdealing2010.pdf (accessed 2010-10-17); for further discussion on the difficulties of proofing the required “intention” in market abuse criminal cases; see Perez, Cochran and Sousa “Securities Fraud” 2008 American Criminal LR 923 925-934; Berwin “Market Abuse: Why the UK’s Approach is Safer than
Markham submits that among all the market-abuse offences, market manipulation is an “unprosecutable crime” due to complexities in proving the offender’s intention.\(^\text{15}\)

According to Becker, reliance on criminal measures imposes a serious burden on government’s public finances and resources.\(^\text{16}\) In addition, Becker argues that criminal sanctions involve: (a) costs that the illegal conduct in question has created; (b) costs of punishment on the offenders, and such offenders suffer a loss of utility which could be deducted from the public and (c) the costs associated with the public criminal prosecution of securities and other offences.\(^\text{17}\)

Another disadvantage associated with the use of criminal measures to prevent market abuse is that the monetary fines or imprisonment sentences that are imposed on the offenders are sometimes insufficient and less dissuasive compared to the illegal gains obtained by such offenders.\(^\text{18}\)

As indicated above, there are divergent views regarding the desirability and effectiveness of tackling market abuse with criminal measures (imprisonment and monetary fines). Some commentators postulate that such criminal measures are necessary to increase deterrence and to uproot market-abuse activities in the global securities markets.\(^\text{19}\) Avgouleas concurs with this proposition and argues further that criminal measures must be complementary used with other enforcement measures like civil sanctions.\(^\text{20}\) This is supported by Moohr who states that the deterrent role of criminal

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\(^\text{15}\) Markham “Manipulation of Commodity Futures Prices-The Unprosecutable Crime” 1991 Yale Journal on Regulation 281.


\(^\text{20}\) Avgouleas The Mechanics and Regulation of Market Abuse 458.
penalties must be encouraged to promote law-abiding conduct in the business world. The authors agree with Moohr’s caution and submission that reliance on criminal measures alone may not be an effective way to discourage offenders from willfully engaging themselves in market activities.

On the other hand, some commentators lament that criminal measures do not deter market-abuse conduct effectively because they are “intrinsically linked to the probability of the imposition of a sanction and the required high level of proof reduces such probability”. This submission is primarily premised on the fact that criminal measures merely treat market-abuse offences as “moral offences”. In addition, Roe and Jackson provide that the public criminal market-abuse enforcement measures are not as efficacious as the private civil measures that are instituted directly by the affected persons in their own private litigation or through regulatory bodies. Alexander also suggests that public enforcement of criminal measures could unduly affect companies and other market participants in doing their business smoothly, hence such measures should be avoided at all costs.

Similarly, Baker disagrees on theoretical and philosophical grounds with the employment of criminal measures or other “law enforcement to stimulate corporate reform and opposes all criminal prosecution of corporations”. The authors disagree with Alexander and Baker’s views as stated above, because they are merely based on the assumption that government and/or courts’ criminal measures for market abuse could unfairly treat corporations and companies differently from individuals in some jurisdictions.

Another view from Avgouleas is that excessive adherence on criminal measures alone to combat market abuse could give rise to “under-enforcement”. This could lead to what Avgouleas refers to as “sub-optimal deterrence”. This was echoed, on the contrary by Coffee who states that the high-intensity enforcement of securities laws could dissuade some investors from entering into their market-related business in some financial markets.

21 Moohr 2003 Florida LR 949-951.
22 Ibid.
23 Avgouleas The Mechanics and Regulation of Market Abuse 454.
24 Rawls “Two Concepts of Rules” 1955 Philosophical Review 3 4-5; Posner “An Economic Theory of the Criminal Law” 1985 Columbia LR 1193; Coffee “Corporate Crime and Punishment: A Non-Chicago View of the Economics of Criminal Sanctions” 1980 American Criminal LR 419 434-435, all these articles outlines that the intense criminalization of market abuse indicates a prevailing view that conduct like market manipulation and insider trading broadly constitutes a “moral wrong”.
29 Avgouleas The Mechanics and Regulation of Market Abuse 456.
30 Ibid. Also see Cooter and Freedman “The Fiduciary Relationship: Its Economic Character and Legal Consequences” 1991 New York University LR 1045 1045-1075, who points out that severe sanctions may be levied less often by courts, “so reducing the probability of the sanction being applied and, hence of wrongdoers being deterred”.

markets globally. The authors concur to some extent with both Avgouleas and Coffee, and they further submit that adherence on criminal measures alone could give rise to the prosecuting agencies being cautious of imposing harsher criminal penalties on market-abuse offenders, which could affect public investor confidence negatively as a result of increased or continued market-abuse violations by some undeterred offenders.

The authors acknowledge the merits and demerits of relying on criminal measures to combat market abuse as discussed above. Yet, they submit, notwithstanding the scholarly views stated above, that criminal measures remain a significant deterrent way of discouraging market-abuse activities. The authors further submit that criminal measures are necessary, and that they must be used in conjunction with other market-abuse enforcement measures like administrative sanctions and civil penalties.

2.2 The role and use of civil measures to combat market abuse

Civil measures are privately employed to discourage market-abuse conduct in many countries. Civil measures like civil penalties, class actions, pecuniary penalties and civil remedies are, in most instances enforced against the market-abuse offenders by specific independent regulatory bodies in different countries globally.

In some instances, depending on each country, civil measures for market abuse are imposed on the offenders and any recovered illicit proceeds will be paid as compensation to all the prejudiced successful claimants. Unlike criminal measures, civil measures require proof on a balance of probabilities that the defendants in question would have committed market-abuse offences. This has, according to Barnes, given rise to more settlements to be achieved in private civil market-abuse cases compared to public criminal market-abuse cases in some countries.
Civil measures carry a number of advantages. Avgouleas argues that the use of civil measures conserve government resources and increases deterrence because of the higher probability of different civil sanctions that could be imposed on the market-abuse offenders. This proposition could have been based primarily on the assumption that independent regulatory bodies do not usually depend on government monetary resources to institute civil proceedings against the market-abuse offenders.

Moreover, civil measures, particularly civil penalties also have some “stigma effect” on the market-abuse offenders. This is what Polinsky and Shavell refers to as a minimal “stigma effect”, which leads to the deterioration of human capital in the case of individuals and loss of reputation in the case of individuals and companies.

Another advantage linked to civil measures is that there is a high probability that such measures will force the perpetrators of market abuse to compensate the affected persons for their losses. Brown states that private and independent regulatory bodies' civil measures have the potential to be very effective compared to public governmental enforcement because they are usually fully self-financed and do not depend on government handouts. Duan lauds the advent of civil measures as an essential way to combat insider trading. This proposition is backed by many commentators. Furthermore, Avgouleas maintains that civil monetary

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36 Avgouleas The Mechanics and Regulation of Market Abuse 468-469; and see further Polinsky and Shavell “The Optimal Tradeoff between the Probability and Magnitude of Fines” 1979 American Economics Review 884 884-885.

37 Polinsky and Shavell 1979 American Economics Review 884-885; and also see Avgouleas The Mechanics and Regulation of Market Abuse 69, who supports that the imposition of civil penalties may lead individuals to lose their employment and/or their reputation, hence they will eventually be stigmatized for their market-abuse conduct.

38 Cox “SEC Enforcement Heuristics: An Empirical Enquiry” 2003 Duke LJ 737 752-757, who states that civil penalties essentially force the perpetrators of market-abuse activities to disgorge their illicit profits to the relevant regulatory bodies, which will then be used to cover the costs of regulation and to be distributed to those who fall victim to such activities.


sanctions or the award of damages transfer the purchasing power or other financial rewards from the “wrongdoer to the taxpayer” and/or the victims of the relevant market-abuse violations. Be that as it may, the authors submit that the main disadvantage of using civil measures is the bureaucracy associated with the victims’ application and claiming of compensatory damages from the market-abuse offenders through the authorized independent regulatory agencies in their different countries.

Other commentators, such as Atkins and Bondi, contend that the advantages of using civil measures to discourage market abuse should be balanced against potential disadvantages of overreliance on such measures alone. The disadvantages that could arise include, inter alia, the possibility of such measures being less deterrent for the purposes of combating market abuse. Moreover, Brown purports that independent regulatory agencies and government enforcement departments must co-operatively use civil, criminal and other enforcement measures to discourage market abuse. The same view is further supported by Rashkover, who notes that civil measures like civil remedies should never be considered as the only law-enforcement tool that can be employed to combat securities fraud and other related violations.

The authors agree with Brown and Rashkover’s views, but they further maintain that employing civil measures co-operatively with other enforcement measures such as criminal and administrative sanctions could effectively remove informational and other barriers that affect the combating of market-abuse conduct globally.

In relation to the comments above, Shen admits that China has not utilized civil enforcement actions very well compared to countries like the United States of America. Although Shen could be right in his proposition, it is submitted that Shen might have been comparing apples with oranges. It is submitted that the United States of America and China’s financial markets’ sizes are different and that this could have influenced Shen’s assessment of the role and use of civil measures in China adversely.

the Securities and Exchange Commission and the Commodity Futures Trading Commission has, to a large extent, successfully relied on civil measures to curb market-abuse practices in the United States of America; and Puri “Enforcement Effectiveness in the Canadian Capital Markets” 2005 Capital Markets Institute Paper, York University 13-15 and 24-28, who acknowledges that reliance on civil measures could encourage more compliance with the securities and market-abuse laws in Canada.

Avgouleas The Mechanics and Regulation of Market Abuse 457; see additionally Perez, Cochran and Sousa 2008 American Criminal LR 925-934, where civil sanctions are discussed as having a remedial, rather than a punitive function.


Moohr 2003 Florida LR 949-951.

See Brown 2004 Ohio State Journal of Criminal Law 532, who argues that civil, criminal and other enforcement measures make the enforcement dynamic and different for the purposes of combating corporate crime.

Rashkover 2004 Cornell LR 546.

Shen 2008 Journal of Business and Securities Law 58, who rightfully notes that a variety of civil measures like bounty rewards, class actions and damages have been successfully used by the Securities and Exchange Commission to address market-abuse violations in the United States of America.
2.3 The role and use of administrative measures to combat market abuse

Relatively few countries have resorted to the use of administrative measures to tackle market-abuse conduct.\(^{48}\) Ranging from one jurisdiction to another, administrative measures include: injunctions; disqualification orders; disqualification actions; asset freezes; unlimited financial fines; public censure; suspension of listing; cancellation of licences; restitution orders; orders for disgorgement of illicit profits; name and shaming; ceasing and desisting orders and costs orders.

These administrative measures may be taken against the perpetrators of market-abuse offences. Notably, such administrative measures are enforced by specific authorised independent regulatory bodies in different countries.\(^{49}\) This entails that administrative measures are sometimes privately enforced by specific independent regulators.

While it remains difficult to state with certainty that administrative measures have improved the enforcement of market abuse due to factors like the differences in financial markets’ sizes and financial resources, a number of commentators agree that administrative measures have to date played a pivotal role in curbing market-abuse activities in different countries globally.\(^{50}\) Enormous progress and advantages associated with administrative measures have been achieved in some countries like the United States of America.\(^{51}\) To add more light on this, among other advantages of administrative measures, the ability on the part of the agencies to make their own rules, regulations and penalties has flexibly enabled more culprits of market abuse to be timeously brought to book.\(^{52}\)

\(^{48}\) Cassim “An Analysis of Market Manipulation under the Securities Services Act 36 of 2004 (Part 2)” 2008 SA Merc LJ 177 195, for a brief overview on the use of administrative measures in some countries. Also see Van Deventer “Harnessing Administrative Law in Encouraging Compliance” 2009 FSB Bulletin 3 3-4.

\(^{49}\) In this regard, the Enforcement Committee is responsible for enforcing the administrative sanctions in South Africa while the Securities and Exchange Commission and the Financial Services Authority are tasked with the similar responsibility in the United States of America and in the United Kingdom respectively.

\(^{50}\) MacNeil 2007 GovNet eJournal 36, argues that the European Community Directive’s move to adopt administrative measures will significantly contribute to the ability, on the part of the enforcement agencies to deter all persons from committing market abuse offences; Wood Regulation of International Finance (The Law and Practice of International Finance Series Volume 7) (2007) 586-590, who acknowledge that specific regulatory bodies in some countries are empowered to institute administrative actions on behalf of the affected persons; Kahan and Posner 1999 Journal of Law and Economics 368, for a further discussion on the use of the “name and shame” administrative method as a direct expression of moral condemnation equivalent of imprisonment and as a symbol of disapprobation and also see Comino 2009 25 http://www.clta.edu.au/professional/papers /conference2009/CominoCLTA09.pdf (accessed 2010-09-14).

\(^{51}\) Hazem The Law of Securities Regulation: Handbook Series Student Edition (1985) 250-252, where the Securities and Exchange Commission was reportedly empowered, as early as the 1980s to suspend, or revoke the registration of the offender companies resulting in many successful disciplinary proceedings against such offenders.

Another advantage of administrative measures, especially unlimited financial fines, is that the persons who incurred losses due to market abuse can claim for their compensation through the appropriate regulatory agencies in their countries. This allows them to obtain such compensation without incurring their own costs of private litigation. Other administrative measures like public censure, disqualification, warnings and disciplinary actions against the market-abuse offenders have the effect of affecting their reputation and forcing them to stop market-abuse practices. According to Armour, reputational sanctions like public censure work much more effectively when regulatory agencies investigate the illicit conduct in question and then publicize the results to the markets. \(^53\) Cancellation of licences, naming and shaming and suspension from listing on the securities exchange may lead other companies and/or investors to reduce their willingness to buy or to do business with the companies associated with market-abuse practices. \(^54\) Alternatively, Armour notes that these administrative measures do not preclude the prejudiced persons from utilizing their contractual entitlements against the securities and/or market-abuse offenders. \(^55\) Asset freezes, injunctions, orders for the disgorgement of profits, restitution orders, costs orders and seize and desist orders have a remedial effect that promotes self-regulation and voluntary compliance. \(^56\) This submission is merely based on the fact the market-abuse offenders would normally want to avoid administrative reputational sanctions and other additional administrative monetary sanctions that can be imposed against them by the courts. \(^57\)

Despite the advantages stated above, administrative measures have their own disadvantages. For instance, administrative measures like naming and shaming and public censure are very difficult to be quantified in regard to their actual impact, advantages and effectiveness in combating market-abuse. \(^58\) In some countries like China, companies that are convicted of engaging in market-abuse activities are obliged to disclose all the details relating to their “public censure” in their annual reports. \(^59\) Nonetheless, the authors submit that, if not managed properly, this public censure may affect the public investor confidence negatively in the Chinese financial markets in the future. Moreover, Moohr asserts that civil administrative penalties for...

\(^58\) Liebman and Milhaupt 2007-2008 Columbia LR 33.
\(^59\) Ibid.
market-abuse or other securities law violations are “problematic because they can implicate due process rights of individuals subject to civil punishment”. Notwithstanding possible constitutional-law implications such as double jeopardy, over-enforcement and/or the undue infringement upon the accused’s constitutional right to justice associated with the use of administrative tribunals to impose unlimited administrative penalties on the market-abuse offenders, it is submitted that Moohr⁶¹ seems to be overly skeptical about whether or not the independent administrative regulatory bodies will be able to enforce market-abuse administrative actions effectively without unduly affecting the involved person’s rights.

Although administrative measures are probably less costly and faster to enforce than criminal measures, it is submitted that they might not be as deterrent as criminal sanctions.⁶² In this regard, administrative measures must be proportionate to the seriousness of the market-abuse offence in question. Put differently, there is some agreement among the commentators that administrative measures are necessary to discourage market abuse in the global financial markets.⁶³ Puri alludes to the fact that administrative measures like remedial orders, forfeiture and administrative penalties must be seriously considered and used more frequently to curb market-abuse activities.⁶⁴ Similarly, Ferrarini notes that there has been a significant shift towards the adoption and use of administrative measures in most European Union member countries.⁶⁵ Lau Hansen acknowledges that administrative measures were incorporated in the European Union market-abuse regime to supplement civil and criminal measures.⁶⁶ Other commentators like Lynch and Moohr argue that administrative measures offer a viable way to ensure compliance, on the part of all persons, with the securities and market-abuse laws.⁶⁷ However, no clarity is given as regards the degree or extent of the

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⁶⁰ Moohr 2003 Florida LR 949-951.
⁶¹ Yet there is some general agreement among the commentators that administrative measures have been enforced successfully by regulators in some jurisdictions, in relation to this see Zibala “Market Abuse Directive French Lessons: France’s Implantation of the Market Abuse Directive” 2007 IFLR 48 48-50; Karmel “The EU Challenge to the SEC” 2008 Fordham International LJ 1692, where the role and use of administrative sanctions to combat market abuse in the European Union was commented on as having been fairly successful; and also see generally Paterson and Kotze (eds) Environmental Compliance and Enforcement in South Africa: Legal Perspectives (2009) 41-102, which discusses and states that administrative sanctions were being used consistently to prevent environmental law violations in South Africa.
⁶² Ferrarini “The European Market Abuse Directive” 2004 Common Market LR 711 737-738; and Ashe and Counsell 2000 New LJ 1344, who maintains that criminal measures are usually used as the principal method of combating market abuse and administrative measures are treated as alternative measures.
⁶⁴ Ibid.
⁶⁵ Ferrarini 2004 Common Market LR 737-739.
⁶⁷ Moohr 2003 Florida LR 949-951; and also see Lynch 1997 Law and Contemporary Problems 34-36, which outlines some theoretical rationale for the use of administrative measures to combat corporate crime.
viability of such administrative measures in curbing market-abuse activities across all the financial markets’ sectors.

Britton and Bohannon admit that administrative measures and enforcement actions are settled rather than litigated. Objectively speaking, both the administrative regulatory agencies and the defendants have significant incentives by opting to settle because an administrative settlement may be more costly and time consuming for both sides. Likewise, Perez, Cochran and Sousa submit that the use of ceasing and desisting orders and injunction orders has been successfully employed by the Securities and Exchange Commission in the United States of America to prohibit an individual or company from continuing with a particular unlawful conduct. In relation to this, monetary penalties, disgorgement orders and other necessary ancillary measures will be taken against any person who willfully violates the relevant federal securities’ laws in the United States of America. It is nonetheless submitted, in agreement with Britton and Bohannon, that injunctions and cease and desist orders must be carefully instituted through the relevant courts to avoid some unnecessary irregularities and the imposition of inequitable sanctions.

Major theoretical questions were raised by Lynch who advocates that administrative remedies are simply used to protect some business classes to protect themselves from the full wrath of criminal sanctions. On the one hand, Sutherland argues, on a sociological basis that administrative measures such as fines were more frequently used to combat corporate misconduct compared to criminal measures like imprisonment. Ferrarini and Lynch, however, stipulate that administrative measures are an extension of criminal measures, hence it is very difficult to draw a clear demarcation between the appropriateness of their role, especially in cases involving insider trading. It is submitted that this possible overlap could result in double jeopardy and other related problems against the market-abuse offenders.

Rose submits further that administrative measures may lead to over-regulation and over-enforcement problems which can affect the required

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68 Britton and Bohannon “PERP’ Walk or Cake Walk? A Study of the SEC’s Enforcement of the Securities Laws Through Agreed Settlements” 2005 Houston Business and Tax LJ 244 256; and also see Pitt and Shapiro “Securities Regulation by Enforcement: A Look Ahead at the Next Decade” 1990 Yale Journal on Regulation 149 179, who postulates that the Securities and Exchange Commission obtains a higher rate of efficient case processing by relying more, on the administrative settlements.


70 Perez, Cochran and Sousa 2008 American Criminal LR 925-934.

71 Britton and Bohannon 2005 Houston Business and Tax LJ 251, states that cease and desist orders are not very different from injunctions, hence they must be consistently and carefully employed.


73 Sutherland “White Collar Criminality” 1940 American Sociological Review 1, questions whether or not there is any clear distinction between civil and criminal measures that are used to prevent market abuse and if such distinction is necessary.

approximate optimal deterrence for market-abuse prohibition negatively. Nevertheless, Rose tends to present a limited view and does not explain clearly how the use of administrative measures can give rise to overdeterrence problems in market abuse and other related cases.

2.4 The role and use of private rights of action and class actions to combat market abuse

The use of private rights of action and class actions is gathering enormous momentum. Some countries have enacted specific provisions that give the persons affected by market abuse a right to seek their own redress and compensation directly from those who commit market-abuse offences. Lyon also identified and acknowledged that in some jurisdictions the issuers of securities and the affected financial instruments are firstly given the private right of action to claim or recover their losses directly from the offenders concerned. Similarly, Ford, Austin and Ramsay maintain that the use of private rights of action is very important because it acts as an additional and alternative enforcement measure against market-abuse activity.

Additionally, class actions are used by regulatory bodies to claim damages from the market-abuse offenders on the behalf of the affected persons. Rose agrees that class actions have been utilized by other countries to claim civil remedies and punitive damages from the market-abuse offenders. Coffee stipulates that class actions are capable, if consistently enforced, to recover “punitive and exemplary damages” from the perpetrators of market-abuse offences. The authors agree with these sentiments from an intellectual point of view and they further submit that private class actions and private rights of action should possibly be introduced in all countries to afford the aggrieved persons additional options to recover their losses speedily directly from the market-abuse offenders. Likewise, Swan acknowledges that private rights of action enables the affected persons to recover their losses from the market-abuse offenders either through the relevant regulatory bodies or through their own private

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75 Rose “Reforming Securities Litigation Reform: Restructuring the Relationship between Public and Private Enforcement of Rule 10b-5” 2008 Columbia LR 1301 1326.
76 Ibid.
77 Duan 2009 Duquesne Business LJ 148, for a detailed analysis on the use of private rights of action in China to curb insider trading.
78 Lyon and Du Plessis The Law of Insider Trading in Australia 221-222.
80 Rose 2008 Columbia LR 1301-1304.
Another advantage of private rights of action is that the prejudiced persons will be able to recover their losses or damages from the culprits involved in market-abuse offences unlike in criminal proceedings for such offences. In the same way, Duan notes that China adopted a “United States of America style” of private actions. According to Duan, private rights of action are important because they are the only way in which the affected investors can be compensated for their market-abuse-related losses.

Nonetheless, Shen questions the effectiveness of the private rights of action for issuers or affected investors in China. Shen argues that private rights of action and class actions for issuers or affected investors might create other economic problems in China due to massive or many class-action litigations that could ensue from such investors. Avgouleas asserts further that the use of private rights of action for issuers or affected investors has attracted some debates among the scholars. Avgouleas submits that private rights of action and class actions for affected issuers or investors could create unnecessary problems and be open to abuse when not managed or enforced consistently. In this regard, Avgouleas maintains that allowing class actions and/or private rights of action to issuers or affected investors to claim damages in market-abuse cases, even if their losses exceed the defendant’s gains has a retributory function. In addition, Rose postulates that class actions for market abuse may lead to overdeterrence on the part of the issuers of securities who face strict liability of their agents or underdeterrence on the part of wrongdoers or market-abuse offenders who could escape liability for their illicit conduct.

Notwithstanding the divergent scholarly views stated above, the authors maintain that it is unfair to deprive the prejudiced persons their private rights.

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83 Brown 2004 Ohio State Journal of Criminal Law 537-541, for related comments on the use of private rights of action.
84 Duan 2009 Duquesne Business LJ 152-154, for more insight on the role and/or use of China’s private rights of action for prejudiced and defrauded investors.
86 Ibid; and also see similar remarks by Choi "The Evidence on Securities Class Actions" 2004 Vanderbilt LR 1465, where theoretical issues and surveys of the evidence on the desirability of securities private class actions and other related problems were discussed.
88 Avgouleas The Mechanics and Regulation of Market Abuse 491, where a submission was made that class actions are characterized by high agency costs because their litigation will possibly be made “in accordance with the lawyer’s economic interest rather than those of the class”.
89 Avgouleas The Mechanics and Regulation of Market Abuse 491.
90 Rose 2008 Columbia LR 1305; also see Easterbrook and Fischel “Optimal Damages in Securities Cases” 1985 University of Chicago LR 611 645 for further discussion and analysis of compensatory damages and class actions; and Dougherty “A [Dis]semblance of Privity: Criticizing the Contemporaneous Trader Requirement in Insider Trading” 1999 Delaware Journal of Corporate Law 83 143, who on the contrary, advocates for the reliance on private rights of action for issuers of securities to prevent insider trading.
of action and class actions to claim their compensation from those who willfully indulge in market-abuse practices.

2.5 The role and use of arbitration and alternative dispute-resolution measures to prevent market abuse

Arbitration and alternative dispute-resolution measures are used to restrict and prevent market-abuse violations in some countries. These measures enable the regulatory bodies to obtain settlements in market-abuse cases less costly and out of court. In other countries, aggrieved persons who might not have been satisfied with the decisions of the regulatory bodies in relation to market-abuse cases may rely on arbitration and alternative dispute-resolution measures for their grievances to be addressed. In such instances, the parties involved (claimants and defendants) are encouraged to reach a consensus on civil remedies and/or punitive damages to be claimed or profits to be disgorged in relation to the market-abuse conduct in question. Furthermore, arbitration and alternative dispute resolution measures offer regulatory bodies a better option to obtain more settlements timeously and less costly. MacNeil argues that arbitration and alternative dispute-resolution measures promote co-operation between the regulatory bodies and the parties involved to either privately settle their market-abuse cases out of court or to publicize their settlement results to the relevant financial markets. Nevertheless, it remains uncertain whether or not arbitration and alternative dispute-resolution measures are deterrent enough to combat market abuse.

According to the so-called strategic theory of regulation, regulatory compliance can be obtained more effectively by dialogue and persuasion rather than the courts’ legal enforcements, since such legal proceedings are expensive whereas persuasive co-operation between the regulatory bodies and the offenders is cheaper. In relation to this, Braithwaite and Ayres argue that arbitration and alternative dispute-resolution measures afford the regulatory bodies a better opportunity to persuade the offenders to desist or stop their illicit activities.

91 For instance, this method is sometimes relied upon in the United States of America.
92 Coffee 2009 Columbia University Law School Memorandum Paper 03/09/09 11 where it was stated that both the Securities and Exchange Commission and the Commodity Futures Trading Commission sometimes rely on arbitration and alternative dispute resolution, especially in cases involving institutional investors.
94 MacNeil 2007 GovNet eJournal 34.
97 Ayres and Braithwaite Responsive Regulation, Transcending the Deregulation Debate (1992) 19-21; also see Rose-Ackerman “Progressive Law and Economics and the New Administrative Law” 1988 Yale LJ 341; and for a further discussion on state regulation
In terms of the “game theory”, regulatory compliance is a dynamic game of negotiation and interaction between the regulatory bodies and the persons regulated. The authors of this article, assert that this game theory might also implies that mutual cooperation between regulators and the offenders concerned is a vital tool for the consistent and successful enforcement of arbitration and alternative dispute-resolution measures, particularly in relation to market-abuse cases.

2.6 The role and use of Chinese Walls to prevent market abuse

Chinese Walls entails the creation of a physical and an operational segregation of functions within a multi-functioning organization or company. This is done in order to minimize and prevent as much as possible the flowing of price-sensitive information from one group of persons or from a department in a company to another group of persons or another department of the same company. Notably, Chinese Walls is sometimes used as a defence that protects juristic persons from incurring strict liability for insider trading or market manipulation as a result of their employee’s unlawful conduct. Nevertheless, for the purposes of this sub-section, Chinese Walls are referred to and discussed only as an enforcement measure used to curb market abuse conduct in different countries.

Gorman notes that segregation of broker-dealer activities or Chinese Walls can prevent insider trading because a “broker-dealer will be unable to obtain inside information from a client through its investment bankers and pass this information on to traders in the retail department”. Additionally, Gorman avows that Chinese Walls can prevent underwriters in a company from imposing undue pressure on analysts to issue favourable reports for the company’s clients and that there is a higher probability that the analysts’ reports will become more objective and reliable for all the investors. Likewise, the authors agree with Cassim who stipulates that Chinese Walls can be both a defence of juristic persons and a mechanism used to prevent insider trading and market manipulation.

Another advantage of Chinese Walls is that it attempts to promote fairness and confidence in the securities markets by ensuring that insiders...
will not be able to engage willfully in dishonest transactions and benefit at the expense of the unknowing investors.\textsuperscript{105} Moreover, according to Nagy, Chinese Walls can reduce the harm that can be caused to potential corporate investors and shareholders when insider trading or other market-abuse violations occur.\textsuperscript{106} The authors submit that this argument is simply premised on the assumption that Chinese Walls prevent market abuse practices like insider and market manipulation and as a result, Chinese Walls preserves the profits of a company’s shareholders and protects them from exploitation by devious insiders.\textsuperscript{107}

Nonetheless, it is submitted that Chinese Walls may, if recklessly used, outweigh the benefits that could be achieved by combining various departments of a multi-functional company.\textsuperscript{108} Evidently, this submission raises questions on whether or not the use of Chinese Walls increases or decreases the efficiency of multi-functional companies in carrying out their functions.

Another problem of Chinese Walls is that it does not completely eliminate all conflicts of interest and instances of market-abuse activities like insider trading.\textsuperscript{109} In relation to this, Gorman gives an example that “an investment banker at one company can just as easily call a friend who is a retail broker for another firm and share inside information”.\textsuperscript{110} The authors agree in part with Gorman’s sentiments,\textsuperscript{111} but they also suggest that the Chinese Walls be employed by the relevant companies in conjunction with watch lists, digital telephonic-data recordings, restricted lists and mandatory disclosure requirements of non-public inside information,\textsuperscript{112} that are internally enforced by such companies to curb market-abuse practices and related conflicts of interests problems.

Gorman further submits that Chinese Walls is more successful only in preventing the accidental flow of inside information than it is in preventing purposeful and intentional disclosure of inside information by insiders to retail traders.\textsuperscript{113} In addition, Gorman argues that the existence and use of Chinese Walls may hinder multi-functional companies from executing their functions and duties well, especially the duty of sharing inside information impartially with all their clients.\textsuperscript{114} Chinese Walls has also been criticized for

\textsuperscript{105} Gorman 2004 \textit{Fordham Journal of Corporate and Financial Law} 488.
\textsuperscript{106} Nagy “The ‘Possession vs Use’ Debate in the Context of Securities Trading by Traditional Insiders; Why Silence Can Never be Golden” 1999 \textit{University of Cincinnati LR} 1129 1152.
\textsuperscript{107} Gorman 2004 \textit{Fordham Journal of Corporate and Financial Law} 489; and also see Jalil “Proposals for Insider Trading Regulation After the Fall of the House of Enron” 2003 \textit{Fordham Journal of Corporate and Financial Law} 689 691-716 which discusses and proposes, apart from Chinese Walls, the use of measures like imposing reporting requirements on issuers (shareholders), transaction registration and incentives to prevent insider trading.
\textsuperscript{108} Gorman 2004 \textit{Fordham Journal of Corporate and Financial Law} 497.
\textsuperscript{109} Gorman 2004 \textit{Fordham Journal of Corporate and Financial Law} 498.
\textsuperscript{110} Ibid.
\textsuperscript{111} Ibid.
\textsuperscript{112} Also see Hermann 18 August 1988 \textit{Financial Times} 23 for related discussion on the disclosure of insider trading for purposes of preventing market abuse activity.
\textsuperscript{113} Gorman 2004 \textit{Fordham Journal of Corporate and Financial Law} 491.
\textsuperscript{114} Ibid.
being “unsuccessful because of the lack of strong incentives for broker-dealers to establish and supervise compliance with them”\textsuperscript{115}. In relation to this, Gorman argues that if a “large firm is unable to share information among its different departments, there are several advantages that are lost. These include cost savings, opportunities for collective thinking and other synergies of combining and integrating various departments”\textsuperscript{116}. Another argument from the opponents of Chinese Walls is that it is extremely inefficient, especially with regard to the work of departmental financial analysts who are obliged under the Chinese Walls to carry out their research duties separately from one another.\textsuperscript{117} In this regard, the authors agree with Gorman,\textsuperscript{118} and they additionally submit that Chinese Walls might create duplication and bureaucracy-related problems that affect the work of the financial analysts and other functions of the multi-functional companies concerned.

Regardless of the concerns and criticisms highlighted above, the authors submit that Chinese Walls should be treated both as a defence and a key enforcement method that can be used to prevent and discourage market abuse practices in different countries.\textsuperscript{119}

3 CONCLUDING REMARKS

This article has discussed six measures that are commonly used to deal primarily with the enforcement of the market-abuse prohibition globally, namely: criminal measures, civil measures, private rights of action and class actions, arbitration and alternative dispute-resolution measures, administrative sanctions and Chinese Walls. Moreover, the significant advantages and disadvantages of each of these approaches were briefly outlined to bring some general insight to the reader on how such approaches might have been utilized to combat market-abuse activity in different jurisdictions. It was noted that each of the stated anti-market abuse-enforcement approaches has different strengths and weaknesses and as such, academics are encouraged to embark on more legal research pertaining to these approaches to increase awareness and enforcement on the part of the relevant stakeholders. Policy makers are also encouraged to engage with the literature on advantages and disadvantages of different enforcement measures in an effort to improve the enforcement measures used in combating market-abuse in South Africa.

\textsuperscript{115} Gorman 2004 Fordham Journal of Corporate and Financial Law 493.
\textsuperscript{116} Ibid.
\textsuperscript{117} Ibid.
\textsuperscript{118} Ibid.
\textsuperscript{119} See Tomasic “The Challenge of Corporate Law Enforcement: Corporate Law Reform in Australia and Beyond” 2006 University of Western Sydney LR 1 4-23, which encourages regulators and companies to focus on, and to devise their own corporate and internal regulatory procedures to improve the enforcement of securities and market-abuse laws.