Insider Trading From Malaysian Law And Islamic Law Perspectives

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What Is Insider Trading?

Bursa Malaysia Securities Berhad (“Bursa Malaysia”) defines insider trading as the purchase or sale of a company’s securities effected by or on behalf of a person with knowledge of relevant but non-public material information regarding that company. The insider is in a position to make massive gains by selling or buying securities before information that might affect the price of the company’s securities (price-sensitive information) is made public.

From this definition, it can be understood that to constitute insider trading, there are three (3) elements that need to be fulfilled as follows:

(a) The trading is effected by an ‘insider’. The insider concept relates to the corporate setting, the word ‘insider’ being one which conveniently describes those who are likely ‘to be in the know’ about significant corporate matters. An insider normally is the one who is connected with the management of company. The insider concept however is also extended to others who forge a relationship with an insider or his company (e.g. by virtue of his employment, office or profession and those who have been tipped off by the insider).

(b) The trading is effected pursuant to knowledge of relevant but non-public material information regarding that company.

(c) The effect of that information is that when it is made available to the public, it will affect the price of the company’s securities.

Position Of Insider Trading Under Malaysian Law

With the passing of the Capital Market & Services Act, 2007 (“CMSA”) in September 2007, the statutory provisions governing insider trading can now be found in Part V, Division 1, Subdivision 1 of the CMSA.

Section 188(2) of the CMSA prohibits an insider in possession of certain information, as described in Section 183, Section 184 and Section 185 from acquiring, disposing of, or procuring, directly or indirectly, an acquisition or disposal of, or the entering into an agreement for or with a view to the acquisition or disposal of such securities.

By virtue of Sections 190 and 191 of the CMSA, the prohibition of insider trading also extends to secrecy arrangements by corporations and partnerships.

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3 Previously, insider trading is governed by Part X, Division 1 of the Securities Industry Act, 1983
Under Malaysian law, if a person commits insider trading, he may be subjected to certain criminal and civil actions, as follows:

(a) Criminal sanction under the CMSA. Criminal prosecution may be instituted against the insider and if convicted of insider trading, he may be punished with imprisonment for a term not exceeding ten (10) years and to a fine of not less than One Million Malaysian Ringgit (RM1,000,000.00)⁴. The only criminal case involving insider trading in Malaysia is the case of *PP v Chua Seng Huat*⁵.

(b) Civil suits by persons affected by insider trading under the CMSA. In addition to and not in derogation of the criminal sanction, the insider may face a civil suit brought against him by persons who suffer loss or damage by reason of, or by relying on, the conduct of the insider⁶.

(c) Civil suits instituted by the Securities Commission under the CMSA⁷. For example, in August 2004, the Securities Commission initiated civil enforcement action against Kuala Lumpur City Securities Sdn Bhd and Wan Azmi bin Wan Abdul Rahman, a former employee of Padiberas Nasional Berhad (Bernas), requiring them to disgorge ill-gotten profits arising from the insider trading of Bernas shares. This resulted in the recovery of Two Million and Eight Thousand Malaysian Ringgit (RM2,080,000.00) from Kuala Lumpur City Securities Sdn Bhd – twice the amount gained by Kuala Lumpur City Securities Sdn Bhd from the insider trading of Bernas shares. Kuala Lumpur City Securities Sdn Bhd and Wan Azmi bin Wan Abdul Rahman were also required to pay civil penalties of Three Hundred Thousand Malaysian Ringgit (RM300,000.00) and One Hundred and Fifty Thousand Malaysian Ringgit (RM150,000.00).

(d) Any civil actions brought against the insider by persons affected by insider trading under any other law⁸.

The CMSA however provides certain defences and exceptions in insider trading cases, as follows:

i. Chinese Wall Defence For Corporations⁹.

ii. Chinese Wall Defence For Partnerships¹⁰.

iii. Exception For Underwriters¹¹.


v. Exception For Corporation With Knowledge Of Its Intention¹³.

vi. Exception of knowledge of individual’s own intentions or activities¹⁴.

vii. Unsolicited Transaction Exception¹⁵.

viii. Exception For Redemption Of Units Of A Unit Trust Scheme Under Buy-Back Covenant¹⁶.

ix. Parity Of Information Defence¹⁷.

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⁴ Section 188(4) of the CMSA
⁵ [1999] 3 MLJ 305.
⁶ Section 201(1) of the CMSA
⁷ Section 201 (5)(6) of the CMSA
⁸ Section 201(11) of the CMSA
⁹ Section 190(3) of the CMSA
¹⁰ Section 191(3)(4) of the CMSA
¹¹ Section 192 of the CMSA
¹² Section 193(1) of the CMSA
¹³ Section 194 of the CMSA
¹⁴ Section 195 of the CMSA
¹⁵ Section 196(1) of the CMSA
¹⁶ Section 197 of the CMSA
¹⁷ Section 198 of the CMSA
Position Of Insider Trading Under Islamic Law

Islamic Law also disallows and prohibits insider trading as it is against several basic principles in Islam.

The said principles are as follows:

(a) **Principles of fairness and justice.** Insider trading is against the basic principles of fairness and justice in Islam as it creates an unfair advantage for one party against other actors in the market. In the Islamic worldview, justice denotes placing something in its rightful place. It also means giving others equal treatment.

   Insider trading is considered as unfair and unjust to others in the market as the culprit has the relevant non-public information which will affect the price of the company’s securities when the information is made publicly available, while the others have no such access to this information.

   Allah says in the *Holy Qur’an* concerning justice and fairness, “Be Fair and Just, that is nearer to piety (Taqwa)”\(^{18}\). In another *Surah*, Allah says, “And act justly. Truly God loves those who are just”\(^{19}\).

(b) **Principle of trustworthiness.** The insider who has access to the privileged information is considered as a ‘trustee’ of that information until such information is made available to the public. Until such time, he is prohibited from dealing with the securities of the company using such privileged information.

   The person who abuses this principle is deemed to have committed a breach of trust. The *Qur’an* and the *Sunnah* of the Prophet Muhammad (pbuh) emphasise the importance of honesty and trustworthiness. Allah says in the *Holy Qur’an*, “Ye that believe! Betray not that trust of Allah and the Messenger, nor misappropriate knowingly things entrusted to you”\(^{20}\).

   It is narrated from Abu Hurayrah by al-Mundhari on the authority of both al-Bukhari and Muslim that the Prophet Muhammad (pbuh) said, “A hypocrite has three (3) signs: when he speaks he tells lies; when he makes a promise he does not fulfil it; and when he is entrusted with something he commits a breach of trust”.

(c) **Principle of entitlement to equal, adequate and accurate information.** Islam attaches great importance to the role of importance in the market. The concealment of vital information (ghish) also violates the norm of Islamic ethics and according to the *Sunnah* of the Prophet Muhammad (pbuh), the informationally-disadvantaged party at the time of entering into the contract has the option to annul the contract.

   Islamic scholars are of the opinion that a transaction must be free from *jahalah* or misrepresentation in order to be considered Islamic. The institution of a transparent market is, thus, quite important and indeed can be considered an Islamic duty and transactions should be executed within the market after taking into account all relevant information.

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\(^{18}\) Al-Maidah: 8

\(^{19}\) Al-Hujurat: 9

\(^{20}\) Al-Anfal: 27