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"INSIDER TRADING IN UE AND US"

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1. Chapter 1 – Insider Trading Regulation

1.1. Introduction

If we think about the world of financial markets and traders, maybe the first picture that comes to light in our mind is a complex vision about a rich life of a trader who lives on the top floor of the highest skyscraper in Manhattan with the best view of New York, who drives the newest model of Ferrari and who makes giant profits from criminal financial trading breaking in someway the regulations. This is the typical life that we can observe in the film "The Wolf of Wall Street", where Leonardo Di Caprio dresses the clothes of Jordan Belfort, or maybe in "Wall Street" and "Wall Street II" through Michael Doulgas as Gordon Gekko, or better yet in "Billions" in the character of Bobby Axelrod. There are several other films or tv series that make our minds to think about the world of trading and finance as a suggestive and maybe illegal world in which criminal and ambitious minds try to become as richer as possible neglecting and indeed facing any kind of law or regulation.

In the real world, market manipulation and illegal securities trading could be observed at many social levels specifically when we are in presence of insider trading situation, the most common violation of the securities regulations. In recent history, insider trading was the centre of a large variety of laws in the field of capital markets in order to protect public investors and shareholders who were victim of trading manoeuvres of corporate directors and CEO for too long. In this elaborate, we want to analyse insider trading laws and how they were executed in different countries starting from the United States of America going through Europe (UK and Italy in particular) and Asia (China and Hong Kong). We would focus on the principal differences comparing each body of laws in Chapter 1, then we try to analyse in Chapter 2 two specific recent cases of insider trading (Netflix insiders) and market manipulation (Elon Musk – Twitter) in order to state how we could rethink and renew contemporary regulations which seems to be too obsolete nowadays.

Insider trading and market abuse had always captured the attention of academic lawyers and economists in many topics concerning corporate law or financial market regulation. Since its birth, the USA always remained the global largest capital market in the world both for the high transactions' number both for the total size and volume of the transactions. As a consequence, the United States was one of the first jurisdictions to forbid insider trading and still now it continues to be the jurisdiction where the ban is most actively enforced. The long history and strongly developed corpus of US law help us to better understand insider trading

doctrine also in all other countries because US laws are the reference global guideline in this field.

1.2. Insider trading in US

1.2.1. Origins of insider trading in US

The problem of insider trading arised in USA as a matter of the state law fiduciary duties of corporate directors and officers. Even after the adoption of the Securities Act of 1933 and the Securities Exchange Act of 1934, federal law had never focused its attention on insider trading until late 1960s. Since early 1980s, a complex federal corpus of laws has emerged as a central key of modern US securities regulation. Today, insider trading doctrine is technically grounded in the federal securities regulation statutes under the Rule "10b-5" emanated by the SEC (Securities and Exchange Commission. However, in the last 30 years the prohibition was executed through a subsequent series of judicial cases in the field of the common law instead of the mere interpretation of the federal statute. As a matter of fact, that series of legal precedents had implicitly created an ad-hoc regulation which has left the entire doctrine with some problems of interpretation.

The current corpus of laws is a product of all the SEC administrative actions and judicial opinions which were executed on the basis of the statutory provision of the Securities Exchange Act -1934, section 10(b) and of the Rule 10b-5[1] of the Exchange Act of 1942. The Rule states that:

> *It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of ant facility of any national securities exchange,*
>
> *(i) To employ any device, scheme, or artifice to defraud,*
>
> *(ii) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or*

[1] 17 C.F.R. § 240.10b-5 Employment of manipulative and deceptive devices

(iii) *To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.*

We can observe that in Rule 10b-5 we do not find "insider" or "insider trading" and literally we can not find any prohibition on insider trading. Nothing in this section explicitly proscribes or prohibits the trading of securities form an individual defined as insider. In fact, in 1934 the Congress addressed insider trading not through section 10(b), even if today it remains the centre of the entire regulations about this theme, but rather through section 16(b)[2]. In details, Section 16 governs transactions by "insiders" of the corporations. Insider is defined as anyone who owns more then 10 percent of any security, or is a director or an officer of the issuer of the security. Section 16 requires that insider must elaborate a statement regarding the amount of securities of the issuers that he owns, at the time of the registration to the SEC or within 10 days after becoming an insider of the corporation. The entire section specifically focuses its attention on short-swing profits from the trading of these individuals only made within six months of registration or acquisition by insiders. We can observe that there is a strong presumption that any profit made with a six-month time period is illegal because of the possibility that insiders took advantage of non-public material information thanks to their position in the company.

In fact, the recent literature on this matter had state that the modern insider trading prohibition have begun in 1961 with the action of the SEC *In the matter of Cady, Roberts & Co*[3]. In this statement, the problem emerged when the board of directors of the Curtiss-Write Corporation decided to reduce future quarterly dividends and one of the directors, mister Cowdin, at the same time was partner of the brokerage firm Cady, Roberts & Co. Before the public announcement by Curtiss-Write Corporation, Cowdin had informed about this important decision one of his partners at the brokerage firm, mister Gintel. After having received this confidential information, Gintel immediately sold a large number of Curtiss-Write stocks held by his costumer accounts where he had the authority to trade. After the public announcement of the dividends cut, Curtiss-Write stocks price obviously lost many dollars per share and Gintel's customers avoided losses in their accounts. For the first time in history, this action had brought to light the practice of the tipping which is the behaviour of an insider who knows confidential information but do not trade himself, but rather than informs (tips)

[2] 15 U.S. Code § 78p – Directors, officers, and principal stockholders
[3] In the matter of Cady, Roberts & Co., file No. 8-3925. Promulgated November 8, 1961

someone else, who trades on the basis of such information. In this case Cowdin was the tipper, the individual who, after having received material non-public information, had warned Gintel (the tepee) in order to take advantage for his customers. In this action, the SEC stated that Cowdin had violated the Rule 10b-5 and articulated what became known as the "disclose or abstain" rule: corporate insiders in possession of material non-public information must always disclose such information before trading or abstain from trading. So the Court opted not to rely on fiduciary principles but rather on a purported policy requiring that all investors must have equal access to information.

1.2.2. Texas Gulf Sulphur

Another historically important action of the SEC regarding insider information was against *Texas Gulf Sulphur Co.*[4] in 1968. The whole action was elaborated around some surveys of an area near Timmins, Ontario by the partners of Texas Gulf Sulphur Co. in March 1959. The company's core business was the mining activity and during those exploration it was found the evidence of an ore deposit. That preliminary survey immediately had demonstrated that there was a significantly concentration of mineral elements like zinc and silver, so the director of the corporation ordered to the exploration group to maintain secret its discovery. In addition, the director hidden that news to alle the other members of the board and employees. Over the next several months, Texas Gulf Sulphur acquired the rights to the land under which this deposit lay after an official chemical assay that confirmed the presence of the minerals. In April 1964, after having denied several "rumors" about previous unofficial surveys, the company announced its discovery publicly in a press conference. Insider trading was detected throughout the autumn of 1963 and spring 1964 when a restricted number of Texas Gulf Sulphur insiders bought stocks and options on the company thanks to the unofficial preliminary confidential discovery previous the public announcement. Other partners tipped outsider individuals in order to trade in advance and make profit from that material non-public information. Moreover, some other individuals accepted stock options from the company's board of directors without informing the directors of the discovery. Also in that circumstance, we are in presence of insider trading and Rule 10b-5 had been violated. The SEC held that when an insider has material non-public information the insider must disclose such information before trading or abstain from trading until the information has been disclosed. The final statement, as the action *In the matter of Cady, Roberts and Co.,* highlighted that the policy of equality of access to information must be respected and all members of the investing

[4] SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d 1968)

public should be subject to the same market risks. The most important conclusion that the United States Supreme Court has promulgated in this action against mining corporation's insider was that anyone who came into possession of material non-public information was required either to disclose it before trading or abstain from trading practice in the affected company's securities.

As we can observe so far, after having emanated insider trading starting laws in 1934, the US regulation have built step by step with consequently actions against corporate insiders a kind of corpus of several judicial rulings emanated with different interpretation of the Rule 10b-5. Firstly, in 1961 the Supreme Court with the final conclusion of the action *In the matter of Cady, Roberts and Co.* for the first time in the history of capital market trading had implicitly promulgated the prohibition in the case of the tipping of confidential non-public material information. Subsequently in 1968, with the action against Texas Gulf Sulphur Co.'s insiders US Court had stated that the founding principle of the prohibition of insider trading is the equality of access to information that could affect market price of securities to all investors in the market in order to not create advantages between market agents and have the same market risks.

1.2.3. Chiarella

In 1979, another action against an individual accused of insider trading had in some way changed the judicial interpretation in the field of insiders about the fiduciary duty implicitly involved between the corporation and the insider which until then was the basis of the entire discipline of insider trading. Substantially, in *Chiarella vs. United States*[5] the United States Supreme Court rejected the equal access information policy. Vincent Chiarella was an employee of Pandick Press, a financial printer whose core business was the production of documents and materials for the disclosure of company takeover bids. During the preparation of these documents, the company used alphanumeric codes to keep the aforementioned companies out of the way and to avoid leaks while respecting confidentiality. Somehow Chiarella managed to break and crack the codes and discover the name of a company for which he was preparing the bidding documents. Before the public disclosure of the announcements of this offer, Chiarella bought shares in that corporation taking advantage of the fact that it had discovered the name. Following the public announcement of the offer, he sold his shares and took a substantial profit from the transaction. Chiarella was therefore

[5] Chiarella vs. United States, No. 78-1202, November 5, 1979

convicted of illegal insider trading on the basis of non-public inside information. However, what has remained in the history of the legislature about insider trading is that the Supreme Court, instead of establishing the violation of the principle of equal access to information by investors, has argued the final sentence through a different point of view. The Court ruled that in this case Chiarella was neither an employee, nor a civil servant, nor an administrator of the company he traded in and therefore he had no fiduciary relationship with that company. Likewise, Pandick Press was in no way a shareholder of the company for which it was preparing the tender offer documents. Therefore, neither Chiarella nor Pandick Press had any obligation to disclose or abstain from trading ("disclose or abstain rule"). Consequently, the Supreme Court could not extend the recognition of the general obligation for all market participants to forgo trading operations based on material non-public information and therefore it had clarified that Section 10(b) can not recognize fraud in the absence of the disclosure obligation given that this obligation does not derive from the mere possession of non-public information. After this ruling, an insider trading policy was therefore reached regarding Section 10(b) based mainly on the violation of the fiduciary duty, omitting the previous mere principle of equal access to information. There are no doubts that *Chiarella vs United States* substantially limited the scope of insider trading prohibition. As such, it posed the fundamental question whether anyone other than classical corporate insiders as directors, officers, and perhaps large shareholders could be held liable for dealing on the basis of insider information.

1.2.4. Dirks

In 1983, the Supreme Court was again called into question in another insider trading action in *Dirks v. Securities and Exchange Commission*[6]. This specific case emerged after the new principle of fiduciary duty recognized by US Court and the case of *Chiarella* still re-emerged as a term of comparison for the sentence. In this action, it was confirmed that the prohibition extended beyond classical insiders and started fleshing out the rules applicable to them. In *Dirks*, the court began by reaffirming its rejection of the equal access standard in favour of a new fiduciary duty-based regime. It stated that there can not be duty to disclose where the individual who has traded on inside information was not a corporate agent, not a fiduciary, not a person in whom the sellers of the securities had placed their trust and confidence. Not to require this kind of fiduciary relationship would depart from the standard doctrine that duty arises from a specific relation between two parties and would amount to recognizing a general

[6] Dirks v. Securities and Exchange Commission, No. 82-276, March 21, 1983

duty between all agents and participants in capital market transaction to forgo actions based on material non-public information.[7]

In *Dirks*, we are in presence of a stock market analyst who was informed by some insiders about the dangerous financial situation of the Equity Funding of America due to a massive impending financial fraud. Based on this non-public information, Dirks believed that the fund would be in dire financial shape and that its market value would drop significantly if the fraud became public. Later, Dirks strongly advised many of his client to sell the fund's stock, alerting them to the information that had been received regarding the upcoming announcements. Once the Equity Funding of America situation has gone public its value precipitated. In this particular action, recognizing that the principle of the fiduciary duty violation in the field of insider trading posed problems for tipping cases like this, the court held that a tippee's liability is derivative of that of the tipper. A tippee like Dirks therefore can be held liable only when the tipper (like the insider of Equity Funding of America in this case) breached a fiduciary duty by disclosing information to the tippee, and the latter known or had reason to known of the breach of that duty.

What therefore emerges from this ruling is that the accusation of insider trading may be due not only to a breach of confidentiality by the insider but also to the failure to comply with the fiduciary duty of loyalty regarding the refraining from making a profit on the basis of the non-public information provided by the tipper. It follows that the most difficult substantive facts for the courts to prove is being able to objectively determine whether the insider tipper benefited personally, directly or indirectly, from disclosing such material to the tippee. As far as the the tipper-tippee relationship is concerned, the simplest circumstance to prove is that of the "quid pro quo" in which the individual who discloses the information in exchange obtains any counterpart in the form of personal pecuniary gain. In other cases, a non-economic return can also be manifested, but rather a gain in the form of personal reputation benefit towards third parties. In 2000, thanks also to the contribution of the conclusions that emerged regarding insider trading and the practice of tipping in *Dirks*, the Security and Exchange Commission began to increasingly adopt a type of interpretation of cases based on fiduciary duty for subsequent accusations and convictions in scope of disclosure of non-public confidential information. Moreover, in the event that an individual acts on behalf of a public company and discloses material non-public information to third parties such as market professionals or securities holders who may trade on the basis of such information, that company is obliged to disclose the same news in a public way. Today, the SEC still

[7] Ibidem at line 654-55

encouraged issuers to make use of the internet and other new information technologies, such as by webcasting conference calls with analyst. Even if the disclosure could be not intentional, as where corporate officers "let something slip", the issuers must make public disclosure immediately after a senior officer learns of the disclosure.

In the last decade, there was a higher development of the SEC's use of the regulation based on fiduciary duty to address information asymmetry in securities markets. One of the most important roles that the Commission attributed to itself is to put many efforts to provide a kind of guidance to corporations and corporate directors about areas of key concern such as the disclosure of information through private meetings and the implications of technological innovations and social media.

As we can observe, *Dirks* and *Chiarella* did not resolve a significant classic case in which an insider of a takeover bidder trades in stock of the target company on the basis of information about the bidder's plans. These individuals are not in whom the shareholders of the target have placed their trust or confidence. In order to provide a unanimous and definitive answer to this type of case, we have to focus our attention on another very interesting rule, Rule 14e-3[8] (d) (1), which explicitly prohibits the insiders of the bidder and target to provide or disclose confidential information regarding a takeover bid to third parties who may thereby violate Rule 10b-5 and trade on the basis of non-public material. It should be noted that this legislation does not prohibit the offeror from the right to purchase target shares or to inform their advisors about their plans, but rather prohibits tipping of information to external individuals who could take advantage of such advice to trade target shares on their own behalf or in turn sub-tip others. There is therefore a substantial difference with respect to the previous disclose or abstain rule or embezzlement rules referred to Rule 10b-5, since here the liability is not based on the violation of a fiduciary obligation. So there is no more need for a showing that the trading party or tipper was subject to any duty of confidentiality or loyalty, and no need to show that a tipper personally benefited from the tip.

1.2.5. O'Hagan

Despite the use of Rule 14e – 3, according to recent literature, the debate on the different interpretations of the Supreme Court in the cases of *Chiarella* and *Dirks* still seemed to remain open. The SEC therefore agreed that it could support a new theory of liability in the

[8] 17 CFR § 240. 14e-3 – Transactions in securities on the basis of material, nonpublic information in the context of tender offers

field of insider trading, namely the doctrine of misappropriation theory. With the promulgation of Rule 14e – 3 it could be implicitly deduced that in general the SEC had limited the misappropriation theory only to cases of public offer and that it could not therefore be used as a doctrine applicable to Rule 10b – 5. Only through the judgment *US v. O'Hagan* of 1997 the SEC ultimately inferred that misappropriation theory could be used as a guiding principle for insider trading crimes in a more comprehensive view on fiduciary liability theory. The *United States v. O'Hagan* accuses Mr. O'Hagan of defrauding the law firm he worked for by misappropriating non-public information for personal commercial purposes. The key driver of the SEC's entire action was Dorsey & Whitney's representation of the Grand Met regarding a potential takeover bid for Pillsbury Company stock. During the preparation of the documents by the law firm, O'Hagan, a partner of the firm, thanks to the confidential information obtained given his position as an insider, began to acquire call options of the Pillsbury shares. Following the withdrawal by the law firm Dorsey & Whitney from the representation of Grand Met, which in the meantime had just publicly announced the start of the public offering for the Pillsbury Company, the price of Pillsbury shares began to rise significantly. Thanks to the timely sale of his call options due to the purchase ahead of the public announcement of the news to investors, O'Hagan earned more than 4 million dollars. The SEC's indictment was primarily based on securities fraud in violation of section 10 of the Securities Exchange Act of 1934, Rule 10b – 5 and fraudulent negotiation of a takeover bid in respect of section 14, Rule 14e – 3. In this specific case, however, the Eight Circuit overturned all convictions on the grounds that the fiduciary liability established by Section 10 (b) cannot be based on the doctrine of misappropriation and that Rule 14e – 3 exceeds regulatory authority of Section 14 because such legislation does not contain any breach of fiduciary duty. In this sense, therefore, the accusations of fraud on the securities addressed to Mr. O'Hagan could not exist. In the final act, the Supreme Court finally held that the criminal liability existing in the violation of the regulations expressed in Section 10 (b) of the Securities Exchange Act may be based on misappropriation theory and that the SEC had rightly and correctly exercised its power pursuant to of Section 14 relating to misappropriation for insider trading.

1.3. General definitions

1.3.1. Inside Information

As we have seen, through the different interpretations provided by the Securities Exchange Commission and the US Supreme Court regarding the main cases of insider trading in the USA between 1934 and 2000, a rather heterogenous set of regulations and laws were reached at the beginning of the twenty-first century on which to be able to judge a convict in matters of insider trading. However, what is more evident is that the entire body of law is based on the illegal use of certain information, considered confidential and non-public, by corporate insiders or people close to them, as such information is essential for being able to gain an advantage on the market over all other investors and market agents. This information is still the main reading key to verify and demonstrate that some individuals can be convicted of insider trading.

Since the beginning of 2000, the regulation of capital markets in the US has therefore tried to focus more attention on objectively defining what "material non-public information" actually is. In defining the term "non-public", US law implicitly distinguishes through the promulgation of Rule 10b – 5 two main forms of information: "inside" information and "market" information. As regards the attribution of the specific term "inside", certain information must in some objective way come from sources or resources internal to corporations and typically concerns facts, events and operational developments that influence or could significantly influence the assets or earnings of the corporation itself. On the other hand, all that certain information that comes mainly from outside sources external to corporations and that in general can have a potential negative or positive impact on the market price of the corporate securities fall within the field of "market" information (so it does not directly affect assets or earnings.

As regards to the term "material", US law states that liability arises only with respect to trading on the basis of material information. Materiality is defined for this specific purpose as whether there is a substantial objective likelihood that a reasonable investor would consider the omitted fact important in deciding whether to invest in securities or not. Moreover, we have to focus our attention to the term "non-public": insiders must not trade whenever they are in possession of material non-public information. The principle of the public disclosure is extremely important and try to overcome the fact that not only insiders, but even public investors must have the same opportunity to act on that information. When such material is disclosed and have been widely disseminated, insider may trade but only after the information

in question has been effectively made public (for example through a press conference, the publication on the official website of the corporation, a video conference open to all investors).

Having therefore clarified what the ban on trading on the basis of material non-public information means, recent literature has still left unresolved the debate or criticism regarding the requirement \ principle of the fiduciary relationship that emerged in various interpretations by the federal judges in judgments regarding the SEC's actions about insider trading violations. As previously mentioned, a too heterogeneous interpretation of the laws has emerged over the years which has led to natural contradictions regarding the requirement to the fiduciary relationship as the founding principle of the crime of insider trading. In neither *Chiarella* nor *Dirks* did the Justice lay out a convincing doctrinal basis for premising insider trading liability on a fiduciary relationship. In fact, the criticism of recent literature reveals a discrepancy regarding the judge's opinion to argue that the common-law duty exists only in "some jurisdictions" and therefore has deemed it his duty to explicitly extrapolate that all insiders are forbidden by their fiduciary relationship from personally using undisclosed corporate information to their advantages. However, this interpretation has raised many issues over the years that are difficult to resolve since, having recognized this judicial position, any individual, in order not to incur illegal crimes in the field of insider trading, would not know whether to turn to federal or US states laws to determine its position in relation to its fiduciary duty in this regard.

In the recent literature on insider trading, the initial intent of the Exchange Act is analysed with respect to its subsequent judicial developments through the judgments and interpretations of the Supreme Court: the main purpose of the promulgation of the articles on insider trading in 1934 seemed to clarify and establish once and for all the idea that being able to abuse certain privileged information by corporate officers or directors could no longer be allowed for their own personal advantage to the detriment of public investors. This idea was at the time considered a very normal additional compensation that undoubtedly belonged to the insiders as a reward for their efforts and their acquired position within the corporations. What was subsequently established in *Cady, Roberts & Co.* was then considered one of the first judicial precedents to be taken as a reference for subsequent and future decisions regarding the crime of insider trading but this ruling, which seems to impose a sort of federal duty that prohibits the insider trading, seems to be in stark conflict and contrast with all the further precedents established by the Supreme Court and the respective positions regarding the federal law of Rule 10b – 5. In particular, there is still today a substantial unresolved

conceptual conflict between the current jurisprudence of the Supreme Court on insider trading and its more general article Rule 10b – 5. This conflict is even more evident in relation to the argument of the judgements in *Cady, Roberts & Co*. and *Santa Fe Industries, Inc v. Green* because in the latter the Supreme Court held that Rule 10b – 5 is concerned with disclosure and fraud, not with fiduciary duties. Moreover, the Court held that Rule did not reach claims where the central key driver of the compliant is that shareholders were treated unfairly by a fiduciary. As we have seen before, in *Dirks* and *Chiarella* it seems that this "doctrinal tension" did not overcome the final interpretation of the cases and Rule 10b – 5 still was the principal fundamental from which state if there was a fraud of insider trading or not. Perhaps in *O'Hagan* we have seen that the Justice have tried to solve that conflict by recharacterizing insider trading as a pure disclosure issue. So, in that case the failure to disclose that an individual is about to inside trade that is the principal problem and misconduct, not even more the trade itself. That approach, as observed before, failed to solve the problem because the final conclusion of *O'Hagan* is that the duty to disclose had to arise out of a fiduciary relationship. So again, if someone have to look to federal law to determine whether a particular relationship is fiduciary or not, he is necessarily invoking a federal fiduciary "standard" whose development *Santa Fe Industries* clearly precludes.

1.3.2. Market Abuse

Although such inconsistency still exists today within US jurisprudence regarding insider trading, there is no doubt according to modern literature that such an offense is nothing more than criminal conduct due to illegal market abuse behaviour. In fact, the entire scenario surrounding this crime is nothing more than an advantage acquired regarding a secret or confidential information of which no one is yet aware and generally in breach of some kind of fiduciary duty. As we had observed before, a certain confusion has evolved over the years due to the inconsistency that seems to permeate the various sentences mentioned above in how we could define unlawful insider trading. One of the major recent criticisms highlights the fact that there has been a strong effort in trying to develop a uniform doctrine based on a coherent and homogenous theory on insider trading by referring too often to the law of fraud rather than more expansive market abuse standard. On the other hand, what is clearly expressed on the basis of the conclusions that emerged regarding the main convictions over the years is the entire set of individuals who can potentially be the subjects of investigations and judicial cases of insider trading. First of all, it is necessary to start from Section 16 (b) of the Exchange Act regarding short-swing profit provisions, which unequivocally indicates that

officers, directors and shareholders owning more than 10 percent of the company's stock. Moreover, after *Texas Gulf Sulphur* the discipline has also been extended to any mid-level corporate employees or to anyone who possesses non-public information even if it does not strictly fall under the term "insider" as defined by Section 16 (b). The universe of potential suspects for insider trading subsequently sees its maximum expansion through the sentences of *Chiarella* where the court referred to any "agent" of the issuing corporation as a proper defendant: all corporate employees are so added to Section 16(b) insiders.

However, some cases of insider trading can also occur in situations where the accused is not necessarily an employee of a company, for example in cases where information about a company is lawfully disclosed to a lawyer, an external consultant, an accountant or an underwriter. In these cases, as emerges in *Dirks*, these outsiders may in a certain way turn out to be fiduciaries with respect to the shareholders as the founding principle for recognizing this duty is that they have undertaken a sort of confidential relationship with respect to the type of work they have conducted with the enterprise business and therefore had access to privileged information for purposes purely related to the company. This fiduciary duty therefore derives not only from the fact that these people have had access to material non-public information, but from the fact that the corporation unequivocally expects that such outsiders will maintain some discretion is not disclosing or using this material for personal purposes and take advantage of the market by trading. However, what is not clearly expressed in *Dirks* is that the individual who receives that information (underwriters, accountants, lawyers, working consultants) should implicitly agree to respect this fiduciary duty relation and keep confidential what he becomes aware of within the company. In this case the literature defines such potential insiders as "constructive insiders" of the issuers, who can potentially be accused of crime by the virtue of their close personal and professional relationship and because of the business context about the issuer's expectation of confidentiality.

In addition, we can also include the so-called tippers and tippees in the circle of possible accused of insider trading. As seen previously in Dirks, tippees could be held liable if it is possible to objectively prove that the tipper breached a fiduciary duty to the corporation by making the tip and the tippee knew or had reason to know of the breach. When these two conditions are met, the requirement that the tip constitute a breach of duty on the tipper's part eliminates many cases in which an insider discloses information to an outsider. Indeed, not every disclosure made in violation of a fiduciary duty constitutes an illegal behaviour is reached if there is a breach of the duty of loyalty forbidding fiduciaries to personally benefit from the disclosure.

1.3.3. Insiders

In *United States v. Chestman*[9], another type of insiders seems to be able to take shape in family relationships such as the relation between wife and spouse. Arguing the ruling in this regard, the Supreme Court has therefore depicted a sort of general guide for the management of those relationships or once that may exist between two so-called non-traditional individuals (i.e., that go beyond the cases of fiduciary relationships described above). The Court can make it expressly clear that in no way will a trust relationship be formed in the event that an individual unilaterally entrusts confidential information to someone, even if it is specifically stated not to disclose it to third parties. Furthermore, it is not possible to define a personal relationship as a family relation of a fiduciary nature if there are no other additional elements. Therefore, clarifying that, for example, a relationship between wife and husband cannot be of a fiduciary nature, the court also expressed its opinion on relationships or associations that instead are intrinsic in nature: lawyer-client, heir-executor, guardian-assisted, principal-agent, trustee-beneficiary, corporate officer-shareholder. In the event that we depart from such relationships, a fiduciary one can arise in the event that one party acts on behalf of the other and there is strong trust one party acts on behalf of the other and there is strong trust or confidence between two parties. In addition, the SEC has once again addressed the issue of non-standard relationships in relation to insider trading and Rule 10b – 5 by stating that there are three main forms of situation where a duty of trust can be encountered for the purposes of misappropriation theory. It is listed as the first situation for which the receiving party of the information somehow agrees to keep this confidentiality secret without disclosing to third parties. The second situation is a natural extension of the first, that is, if there is a model or practice or a document between two parties that certifies a sharing of such information in such a way that the provision of it is expected on its part to be an obligation of confidentiality. Finally, it is expressly specified that this obligation also exist between a spouse, parent, child, or sibling when one of these individuals receives material non-public information.

1.3.4. Congress Insiders

In recent years, recent studies have also paved the way for a final type of potential insiders who had never been the subject of investigations or even potential accusations in this regard

[9] 947 F.2d 551 (2d Cir. 1991)

until the early 2000s: members of the American Congress and legislators. It seems almost impossible that the very people who should legislate on insider trading are themselves capable of committing this crime to the detriment of the investors and individuals their laws are supposed to protect. Regarding this situation, the study that has generated the most chaos and confusion is the 2004 analysis conducted by Alan J. Ziobrowski, Ping Cheng, James W. Boyd and Brigitte J. Ziobrowski. In this paper[10], the authors were able to demonstrate that on average American Senators were able to "beat" the market by about 12 percentage points per year, indicatively between the 1990s and 2000s. This result is even more surprising when compared to the two other estimates emerged from the paper, namely that households on average underperformed the market by 1.4 percent a year and even "traditional" corporate insiders on average beat the market by only 6 percent a year. As it can be seen, not only have these legislators committed insider trading crimes but, moreover, they have been able to obtain personal profits which, on average, turn out to be double the same profits generated by illicit conducts by corporate insiders. In the last twenty years we have therefore found ourselves in a situation of public scandal such that the same guardians of the laws in the field of insider trading were at the same time legislators and criminals of it. The conclusions of the authors of the aforementioned study trace this illegal behaviour to the fact that some Senators were able to have access to material non-public information about the companies in whose stock they trade. In their analysis, they show that the most interesting fact about trading these stocks is the timing: by studying the behaviour of cumulative returns it seems that Senators knew exactly the perfect time to buy or sell their holdings. The researchers stated that you don't even need to have such a fervent imagination to understand that Senators, during their tenure, can have earlier access to relevant information than other investors thanks to the advantage gained from their role as legislators.

Indeed, members of the Congress can obtain material non-public information in many ways and in different situations. Firs of all, they can acquire "inside" information when strictly situations and confidential facts about a company are disclosed during a federal investigation or Congressional hearing. However, there seem to be more frequent cases of insider trading regarding "market" information (which differ from inside information as explained before) which Congress can benefit from situations such as recommendations of investment advisers, unloading shares by a large stakeholder, tender offers, or even being able to know in advance which particular corporations will benefit from the approval of a regulation regarding taxes or

[10] Abnormal Returns from the Common Stock Investments of the U.S. Senate, Alan J. Ziobrowski, Ping Cheng, James W. Boyd and Brigitte J. Ziobrowski, Journal of Financial and Quantitative Analysis, 2004, vol. 39, issue 4, 661-676

the tax authorities. This practice of governmental insider trading has recently been the subject of public debate, which then resulted in a public complaint as if it were a form of corruption at government levels. In 2012, with President Barack Obama's signature on the Stop Trading on Congressional Knowledge Act[11] (STOCK Act), there finally seemed to be a stringent stance on trying to stop and regulate this type of illicit conduct that permeated the American government apparatus. This act was adopted in USA in response to the allegations discussed above of insider trading by members of the Congress on the basis of confidential information obtained through their elected position and try to bring back the public alarm that was spreading more and more in American citizens vis-à-vis the legislators.

As often happens in many political situations, to attract and engage the attention of the general public and the mass media it takes a shocking or not ordinary event. In March of 2020, many lawmakers came under fire for selling major holdings at the start of that year's stock market sell-off. A striking example of this are Senators Richard Burr, Kelly Loeffler, Dianne Feinstein and James Inhofe, who have been accused of repeatedly abusing the use of inside information to make personal profits from the stock market. These accusations have literally opened the eyes of many journalists and reporters to a world of which still too little had been said. To address these charges, the aforementioned Senators had to resign from the Senate and face their own personal sentences. It is useful to remember that until the outbreak of the 2008 financial crisis, legislators were subject to few restrictions regarding the ability of Senators and members of the chamber to be able to exchange individual shares and in fact the general public was not in the least concerned. Many criticisms, in fact, define the enactment of the STOCK Act of 2012 as a real attempt to "clean up" Washington in the eyes of the world and global financial markets. However, what is debatable is the fact that the stock act is actually enforced by the US Department of Justice and the Securities and Exchange Commission, but they get their own funding from Congress, that is, from the very body they are supposed to regulate. It is therefore inevitable to affirm that there is a real conflict of interest between the parties and that instead of putting "rumors" about the continuous insider trading abuse by lawmakers once and for all, the STOCK Act has actually caused even more confusion as to the transparency and main purpose of this legislation. As discussed from the beginning of this chapter, the Securities Exchange Commission defines insider trading as buying or selling a security in violation of a fiduciary duty or other relationship of trust while in possession of non-proprietary material non-public information about securities. However, what is still difficult to understand today is that insider trading is not a playing field limited

[11] S. 716, signed into law on April 15, 2013, Public Law 113-7

only to wealthy financiers or celebrities but rather this field has also been too open recently to its own regulators and authorities. Indeed, politicians have a unique vision of what most individuals do not have, as the scale and scope of what the Congress is involved in on a daily basis, be it issues related to health care, defense, markets, financial information, are all substantial material that can potentially move the market at any time. Taking up the aforementioned 2004 study conducted by the group of professors and researchers, it is obvious that the profits generated by lawmakers' trading are not in the least comparable to that produced by corporate insiders and this is due to the fact that they have access to privileged information in best timing ever to be able to profit from it. As early as 2006, STOP Trading was introduced on the Congress Knowledge Law which, as its constitutive purpose, would prohibit the Congress members and employees from profiting from non-public information obtained through their public official roles. To have an even more striking example of the abuse of insider trading by American lawmakers, we must refer to an exposition in the Washington Post according to which 35 members of Congress, during the financial crisis of 2009, collected the information received from meetings with the secretary of the Treasury Hank Paulson deriving huge profits in the negotiation phase of their holdings. Finally, a 2020 study published in the Journal of Finance showed that there is objective evidence of abnormal business practices exactly 30 days before the US Government dislocated economic stimulus funds during the 2007-2009 financial crisis. These practices were then used as objective evidence of convictions pronounced against corporate insiders strictly in connection with Congressional politicians.

It is clear that the principle on which the Stock Act was founded is that members of the Congress are in an official public position which necessarily implies a fiduciary duty towards the government of the United States of America and with respect to the American citizens themselves. The bill was so necessary to give a strong signal of firm condemnation to the abuses of insider trading among Senators that it passed clearly overwhelming with 417 votes in favour against 2 in the House and 96 in favour against 3 in the Senate (including 3 unfavourable votes are also found Senator Burr). Burr's vote was further evidence that he was guilty of insider trading when news spread in March 2020 that 4 US Senators (including Burr) were under investigation for insider trading. The crime charge was based on the fact that Burr, well before the drastic escalation of the coronavirus, had publicly reassured citizens that the USA would in any case be perfectly prepared for the arrival of the pandemic both at the socio-health and economic-financial level, despite certainly knew during the January 24, 2020 briefing with the Senate Health Committee, CDC Director Robert Redfield and White House

Pandemic Advisor Anthony Fauci, that the upcoming COVID-19 would have devastating effects on the economy and on the health and insurance sector far worse than any other pandemic seen before. After Burr's public disclosure of the strong stability of the US economy despite the impending outbreak of the pandemic, the Dow Jones Index set an all-time high by reflecting Burr's information directly to US market investors. On February 13, taking advantage of this situation, Senator Burr sold between 630,000 and 1,7 million dollars of investments in 33 separate transactions without buying even a single share, a clear sign of complete distrust by Burr himself of what he had publicly communicated to all the American people and globally about the stability of the American economy. Moreover, Burr could also have been accused of the practice of tipping, according to what was published by ProPublica and some rumors regarding telephone conversation recorded by NPR, as he would have strongly advised his brother-in-law and other friends regarding the divestments, he would have made in the future in order to make they too could profit from this privileged confidential information. Another young senator was accused of the same offense, Kelly Loeffler, as she too attended the same aforementioned briefing along with Burr. In the two weeks following the meeting, she and her husband Jeffrey Sprecher (CEO of Intercontinental Exchange and president of the New York Stock Exchange) sold shares and holdings for a total amount of between 1,2 and 3,1 million dollars, very similar to what Burr had just done. During this SEC investigation, Joe Biden's presidential election campaign in July 2020 was heralding that one of the party's first manoeuvre would be to ban stock trading by all members and staff of Congress. However, this decision seems to have been the result of a timely reaction by Biden to the public accusation by the SEC against illegal insider trading by American lawmakers during the lockdown caused by the coronavirus (another way of strengthening the position of members of the American Congress in the eyes of international investors). Even Donald Trump's campaign team refused to answer any questions by CBNC about this and his stock exchange policy. Historically, members of the American Congress have always believed that the best possible control over conflicts of interest and governmental insider trading was the fact that of compulsory re-nomination and elections every two years and have always believed that disclosure, as well as accountability that comes from holding elected office, was more than enough control to prevent them from deriving any financial advantage from their federal roles. As we have just been able to observe, this historical assumption seemed only to be a protective shield behind which to take refuge in order to actually take advantage of this conviction and allows insider trading at the legislative level.

In 2018, Senator Elizabeth Warren proposed a radical new legislative package on the subject of conflict of interest in insider trading among congressman: the Anti-Corruption and Public Integrity Act[12]. The Senator's primary purpose was to effectively eliminate the influence of monetary gain via trading at the federal government level. The ultimate goal was to be able to unequivocally prohibit elected officials and senior agency officials from owning and trading company shares while they are in public office. According to Warren's opinion, lawmakers would finally have thought exclusively about the good performance of the American market once they were free from the possibility of manipulating and obtaining substantial profits through the criminal use of the confidential information they would receive daily during their office. Another proposal for a bill advanced in 2018 was that of Senators Brown and Merkley, concerning the prohibition of lawmakers from being able to hold individual shares in individual companies and at the same time being able to vote on issues that concern the same companies and the inevitable conflict of interest that in naturally created. In 2021, Senator Warren's bill passed in the Anti-Corruption and Public Integrity Act divided into six main Titles. Title 1 mainly refers to strengthening the public integrity of lawmakers through the elimination of financial conflict of interest as American citizens must always be protected and be confident that the actions taken by their governors are always in the service of the citizens themselves and not of the member of the Congress or political forces. In order to eliminate such potential conflicts, it is expressly banning individual stock ownership by lawmakers, Cabinet Secretaries, federal judges and staff, White House members and all other senior agency officials while in office. Moreover, they may under no circumstances hold or trade in stock where its value could potentially be influenced by their agency or departments. The Presidential Conflicts of Interest Act is also established which requires that President and Vice President must place conflicted assets into a blind trust to be sold off. In order to strengthen public integrity in the eyes of citizens and international investors, it is required that all senior government officials and all White House staff must divest from privately-owned assets that may represent conflicts of interest such as multinationals or commercial real estate. There is also a first attempt to apply defined ethical laws to all employees of government bodies and the creation of a so-called conflict-free investment portfolio for federal officials with new investments accounts managed by the Federal Retirement Thrift Investment Board and conflict-free mutual funds. Another point on which it is worth paying attention is that relating to the attempt to close the "Revolving Door" between American corporations and the government, or to prevent any attempt by companies and multinationals to gain influence within the members of Congress or to profit through the public service of federal officials.

[12] H.R. 9029 – Anti-Corruption and Public Integrity Act, 116th Congress (2019-2020)

Among the numerous points of Title 1, the absolute prohibition for life on the exercise of pressure or attempts to lobby by the President and Vice President, but also by all members of Congress including Cabinet Secretaries and federal judges, stands out. It is even expressly forbidden to the largest companies in the world, including banks, multinational monopolies, measured on the basis of average annual revenues and their market capitalization, to hire or have professional-working relations with individuals who have at least up to 4 years before exercised government official positions after they left their role. In a final analysis, it is also necessary to point out for the first time in history the ban on the so-called "Golden Parachutes" which provided substantial corporate bonuses to executives for the federal service. In Title II, on the other hand, we have a real public accusation against lobbyists for putting an end to the practice of lobbying in federal circles. Lobbyists are defined here as all individuals who have been paid or obtained in return for financial gain to influence the government or federal authorities. An attempt is therefore made to put an end to the corruption of the so-called legalized lobbyists by exchanging money with federal government favours in order to increasingly strengthen the independence of the Congress from lobbyists and people of influence to ensure transparency and integrity to federal bodies. Title III attempts to de-politicize the rulemaking process and increase transparency of industry efforts to influence federal agencies through various guiding points regarding the elimination of loopholes that allow corporations to tilt the rules in their favour against the public interest. With the guideline of the protection of the interests of individuals to defend in cases of federal lobbying and insider trading at government level, several articles are then deliberated on increase the ability of the public to make sure their interests are always considered when agencies act and provide them with tools and resources to implement strong rules that reflect the will of Congress and protect public. Moreover, Title IV specifically concerns federal judges and their role in federal justice. In fact, an attempt is made to enhance the integrity of the judicial branch by strengthening rules that prevent conflicts of interest, for example by banning individual stock ownership by federal judges or by enhancing public insights into the judicial process by increasing information about their sentences and reducing barriers to accessing information. The last two Titles instead deal with the effort to create a single and independent agency dedicated to enforcing federal ethics and anti-corruption laws and boost the transparency in federal bodies through the disclose of basic tax return information for candidates for federal elected office.

1.4. US model in the world

As regards the analysis of the extra-US regulations in the world concerning insider trading, it must be immediately specified that, as mentioned at the beginning of the chapter, the American financial market and its regulatory structure have always been historically taken as a model on which to outline a regime of laws that was able to live up to the US standard. What consequently emerges from the recent literature is that the primary factor for shaping an efficient economic/financial development in a country is an effective legal regime for the protection of investors that puts their trustsheep at the centre of the body of laws. This part of the chapter will therefore highlight the fact that global regulation in various countries such as the United Kingdom, China and India, has few differences in terms of substantial legal discipline compared to the US one, but the purely formal legal norms (although very similar between the various countries) can be very different from reality of actual practice, especially in rapidly growing and developing economies such as China and India. Much research on the real effectiveness of insider trading regulation demonstrate that the turning point in many countries is not the fact of having or not a developed body of laws on insider matters but rather whether these laws are actually applied in reality through the specific dedicated judicial authorities.

1.4.1. China

The current regulatory regime in China concerning the financial markets is structured on the basis of the sectoral principle, i.e., there are three different types of judicial authorities, each of which is specialized in overseeing a specific sector. The first authority's organism is responsible for the regulation and the national authority on the securities and futures markets, the China Securities Regulatory Commission, and it is precisely to this Commission that the role of combating and regulating insider trading is also assigned. The other two commissions deal with regulating the banking and insurance sector, the China Banking Regulatory Commission and the China Insurance Regulatory Commission. From the recent literature on financial regulation in China, it can be inferred that the first steps towards enactment of a body of insider trading laws were taken around the early 1990s when the Chinese stock market was in its infancy. As mentioned earlier, China has also relied heavily on the US model to be able to provide a developed regulatory regime regarding insiders and today we can find the key provisions on this matter within the Securities Law of the People's Republic

of China[13]. This law has dedicated much attention to the issue of insider trading which we find in five articles which mainly summarize the definition of insider, the issue of privileged information and all types of prohibited activities which constitute a crime. We also find further indication on the matter in the act issued jointly in 2012 by the Supreme People's Court and the Supreme Prosecutor's Court which provides more details and describes various guidelines on the specific management of criminal insider trading cases ("Judicial Interpretation on the law of Insider Trading in Criminal Cases"). In addition to these main regulatory provisions, there are further ancillary provisions that indirectly regulate insider trading as they are in effect preventive measures against the crime itself. We find an example of these measures in Article 142[14] of the Commercial Company Law of the People's Republic of China which stipulates that "traditional" insiders such as directors, supervisors, senior managers (as in the US regulatory regime) cannot in any way sell shares they own of their company within one year of listing and within six months of their resignation or dismissal from the company. Another preventive measure very similar to the US model is Article 3 of the announcement regarding the regulation of the disclosure of companies listed on the markets and the responsibility of "Relevant Interested Persons". This rule states that in the planning and design phase of events deemed relevant or potentially having an effect on the price of a company's stock, individuals who may come to know of this project or planning such as for example the usual "traditional corporate insiders" or even subjects directly involved in the planning phase have an absolute obligation of confidentiality until the public disclosure of this event\project.

Finally, we find a further rule that seems to recall section 16 (b) of the Securities and Exchange Act of 1934 in the US, i. e. the absolute prohibition of short swing trading: all directors, managers, majority shareholders and supervisors of a listed company must compulsorily return to it any short-term profits realized thanks to any purchase or sale of shares and derivatives of the company in the previous 6 months.

There is no doubt that, compared to the historical capital markets of Western Countries, the Chinese security market is much younger, and it is bipartite between the Shanghai Stock Exchange and the Shenzen Stock Exchange, both born in the early 1990s. Although they were born later than the American and European markets, in their short history Chinese markets have played a very important role in the economic and social growth of the entire country

[13] Securities Law of the PRC, (promulgated by the Nat'l People's Cong., 29 December 1998, effective 1 July 1999)
[14] Company Law of the PRC, (promulgated by the Nat'l People's Cong., 29 December 1993, effective 1 July 1994) art. 142

thanks also to the considerable progress and developments since the 2000s (today the Chinese market is ranked as the second largest securities market in the world by volume and size). As it is easy to imagine, hand in hand with the remarkable and exponential economic development of the Chinese markets, the possibility of inside trading has in turn increasingly expanded, especially after 2010, the year of maximum expansion of the Chinese economy. Many studies since the 2000s explain how insider trading was widespread in China due to poor regulation that failed to develop in tandem with the enormous growth of domestic markets. Another factor that encouraged the growth of insider trading cases was certainly the decision to establish the so-called GEM, Growth Enterprise Market, at the end of 2009, in parallel with the implementation of a short-sales and margin lending system and the introduction of index futures between 2009 and 2010. These remarkable and sudden developments in the Chinese market system have therefore also consequently increased trading and insider trading opportunities.

To date, the practice of insider trading in China is regulated in a similar way to that of the United States. The primary insiders are therefore examined as the centre of the possible conviction of insider trading and then the responsibility is extended to all individuals who have made trading on the basis of information obtained illicitly. Articles 73[15] and 74[16] of the Chinese Security Law prohibits in general terms individuals with knowledge of inside information from using such material to trade securities and moreover list some specific types of individuals that are considered by the law to be insiders (i.e., persons in possession of inside or confidential information). These Articles proceed with an index which divides and categorizes statutory insiders in many groups. Similar to US legislation, we find the first group which includes corporate directors\officers and supervisors\managers, then we have the secondo one which is characterized by the presence of members of senior management and lower-level employees of the corporation. Finally, we have another group of traditional-statutory insiders which is the one dedicated to substantial shareholders of the company. In addition to this, Chinese legislation adds two more groups of individuals that are listed as insiders: one group encloses the so-called temporary insiders in US law, that is nominal outsiders who participate in securities trading such as accountants, consultants or staff members, the second one refers to individuals who have regulatory authority over securities trading.

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[15] Securities Law of the PRC (promulgated by the Nat'l People's Cong., 29 December 1998, effective 1 July 1999), art. 73

[16] Securities Law of the PRC (promulgated by the Nat'l People's Cong., 29 December 1998, effective 1 July 1999), art. 74

In addition to articles 73 and 74, Chinese legislation introduces also the misappropriation theory (again similarly to US) in order to expand the scope of its insider trading regulation. The Judicial Interpretation of Insider Trading Law in Criminal Cases combined to Article 76[17] of Chinese Security Law give us the general application of insider trading in China. A person could have illegally obtained inside information in three specific circumstances: through cheating, tapping, spying, extraction and private trading; from the close relatives of primary statutory insiders; from people who have contact with primary insiders during the sensitive period of the inside information.

Regarding the definition of insider information in Chinese law, we find the general statement in Article 75:

Inside information is information that is not made public because, in the course of securities trading, it concerns the company's business or financial affairs or may have a major effect on the market price of the company's securities.

In order to give a better guideline to the application of this vague definition, Article 75 (2) lists some specific types of fact that are objectively defined as inside information. In this various index we find major events and changes concerning for example the distribution of dividends or in company's equity structure or debts, potential liability for major damages to be assumed by the company or plans concerning the takeover.

In China, the precondition for those to be considered as insiders is that they possess inside information but, for insider trading liability to occur, the necessary element is the defendant's knowledge of the nature of that information, more accurately, if it is material and non-public. Chinese legislation provides two possible tests for proving this knowledge of inside information: the subjective knowledge test and the objective knowledge test. While it is logical and easy to understand in theory, the possession requirement is in practice one of the biggest problems to prove facing Chinese regulators in fighting against insider trading. In the last decade, the CSCR tried to solve the issue by exploring the possibility of reversing the burden of proof. Therefore, in 2012, the newly issued Judicial Interpretation on Insider Trading Law in Criminal Cases stated the presumption of possession of inside information for the types of insiders listed in Article 74. These presumptions of possession can be rebutted if the defendant can demonstrate that they have justifiable reasons or information sources for the seemingly transactions. In addition to this, we have to clarify whether the imposition of

[17] Securities Law of the PRC (promulgated by the Nat'l People's Cong., 29 December 1998, effective 1 July 1999), art. 76

liability presupposes a further showing that the insider actually used the information. This issue is very similar to the debate analysed previously in the Chapter about US legislation, in particular the possession or use debate. In order to give a final answer to that debate, the CSRC's position provides that a transaction conducted by individuals in possession of inside information would not be treated as insider if the transaction is conducted according to pre-existing contract, plan or based on legal source of information.

As mentioned earlier, the body of law governing insider trading in China has been heavily influenced by foreign legislatures, especially that of the United States. However, probably due to the exponential growth of the domestic market in a few years, Chinese legislators seem to have grouped a series of American standards and articles in a copy-and-paste manner without however paying adequate regulatory attention to how they relate to each other and how they have to be applied in practice. As analysed above, the US legislature itself has undergone enormous modifications and changes over time starting from Rule 10b-5 up to the sometimes-conflicting theories of responsibility and equal access to information finally approving the theory of embezzlement to complete the classical theory.

In China, Article 73 generally provides that any person with knowledge of inside information is expressly prohibited from trading securities by taking advantage of such material. In this case, it seems that the Chinese legislature has adopted the American model of equal access to information which however contrasts with articles 73 and 74 which instead index who are the insiders (similar to the classic US theory in Chiarella and Dirks). In article 76, on the other hand, we could observe the introduction of a theory of misappropriation similar to the US system with reference to individuals who obtained information illegally. In conclusion, it seems that Chinese lawmakers have tried to adapt as best as possible to the standard US system of insider trading regulation without having fully understood the logic of the functioning of the US regime as a whole in theory and practice.

1.4.2. United Kingdom (UE)

Both insider dealing and market manipulation have been recognized as criminal offences in all European Economic Area countries and in most other jurisdictions with developed financial markets. The European Union Directive[18] on Insider Dealing and Market Manipulation requires EU members states to create a civil offence for insider dealing and market manipulation known as Market Abuse offence.

[18] Directive 2003/6/EC of the European Parliament and Council of 28 January 2003

Similarly to what we have highlighted in the part dedicated to US and China, also in the United Kingdom insider dealing can be defined as trading in organized securities markets by persons in possession of material non-public information. Insider dealing is a criminal offence defined since 1993 in Part V of the Criminal Justice Act[19] while market abuse is a civil offence stated by the Financial Services and Markets Act 2000[20]. The regulation of insider trading in UK and UE, like China and US, had the main objective of protecting shareholders against the misuse of confidential information by corporate insiders who are in position to gain at the expense of the company and its shareholders. Until 1980, the restrictions on insiders in the United Kingdom were extremely limited due to the fact that the only requirement in the Companies Acts[21] for directors and shareholders was to report dealings in the shares of their companies. The most significant element of regulation was provided by a range of self-regulatory and professional bodies in the City of London, like the City Panel on Takeovers and Mergers or the London Stock Exchange. As years go by, the self-regulatory bodies increasingly recognized that statutory powers were required, in particular where there were international parties in the transactions. The discipline of criminal liability for insider dealing offence was born under Part V of the Criminal Justice Act 1993 by expanding the definition of the term "insiders" and "securities" as the result of the UK Government's implementation of the 1990 European Community Insider Dealing Directive[22]. This directive tried to highlight three main classes of behaviour and circumstances to prohibit: dealings in price-affected securities based on inside information; forcing other individuals to deal in price-affected securities thanks to inside information; knowingly disclosing inside information to other persons. The CJA 1993 directive combined to the UK Financial Services Act 1986[23], which regulates market manipulation, give us the traditional approach to control insider trading under criminal law. In order to better understand how the Criminal Justice Act 1993[24] works, we have to focus our attention specifically on its Part V under § 52[25] which provides a kind of prevention from the crime of insider dealing and insider trading:

[19] Criminal Justice Act, 1993. UK Public General Acts, 1993 c. 36 – Part V

[20] Financial Services and Markets Act, 2000. UK Public General Acts, 2000 c. 8 – Part VIII Section 118

[21] Companies Act 1980, UK Public General Act, 1980 c.22

[22] Council Directive 89/552 of 13 November 1989 co- ordinating regulations on insider dealing, 18 Nov. 1989, L 334/30.

[23] Financial Services Act, 1986. UK Public General Acts, 1986 c. 60

[24] Criminal Justice Act 1993, c. 36

[25] Criminal Justice Act, 1993. UK Public General Acts, 1993 c. 36 – Part V – The offence of insider dealing – Section 52

(i) An individual who has information as an insider is guilty of insider dealing if, in the circumstances mentioned in subsection (3), he deals in securities that are price-affected securities in relation to the information

(ii) An individual who has information as an insider is also guilty of insider if

a. He encourages another person to deal in securities that are … price-affected securities in relation to the information, knowing or having reasonable cause to believe that the dealing would take place in the circumstances mentioned in subsection (3), or

b. He discloses information, otherwise than in proper performance of the functions of his employment, office or profession, to another person

(iii) The circumstances referred to above are that the acquisition or disposal in question occurs on a regulated market, or that the person dealing relies on a professional intermediary or is himself acting as a professional intermediary.

The above definition spokes about "individual", this term is used to distinguish between individual people or persons and corporations or other entities like for example public authorities. Therefore, the criminal liability here may only attach to an individual and then, only with a secondary offence, could attach firms or company comprising a collection of individuals. It follows that, a public authority or a corporation could be liable for insider dealing only by committing the secondary offence, i.e., encouraging another person to deal (point *(ii)*, *a* of the previous definition).

Moreover, very similarly to what happens in US and China legislations, also UK lawmakers have made a distinction between primary insider, who has direct knowledge of inside material, and secondary insider, who learns inside material from the primary). Exactly as US and China laws, also for UK legislation primary insider are listed as directors, employee and shareholders, while secondary insiders are defined as any individual who obtains material non-public information directly or indirectly from a primary insider. As we have mentioned before, there are two essential requirements for the dealing offence, i.e., an individual must have inside information, and he must deal in securities that are price-affected in relation to the information obtained. It is not difficult to notice that there are a parallel guideline with respect to the US legislation because the term "price-affected" refers to securities' prices that may be significantly influenced by the inside information if it would be made public. Moreover, the securities to which the normative refers to as "price-affected" are indexed and well defined in

the Schedule 2[26] of the Criminal Justice Act of 1993: shares, debt securities, warrants, depositary receipts, options, futures and contracts for differences. We can see that this list includes both shares and debentures in companies, both their derivatives but also contractual rights or local authority stocks. The index is perfectly uniform to the European Directive on Insider Dealing[27] and its consequently regulatory changes which covers not only corporate securities and derivatives but also contractual rights in futures and derivatives.

The concept of "insider dealing" is broad enough to encompass all those who, thanks to their position in the company or their business\professional relationship, are likely to have privileged access to confidential or secret information. So, the classical example of the US legislation on primary insiders like a director of a company who misused the confidential information he could obtain can still be bought back in UK legislation on insider dealing. If the director of the example manifestly trades on the basis of inside information he misappropriated it, in terms of US federal law, and then we could apply the discipline of insider trading.

As mentioned before, we still have a parallel guideline between UK/UE legislation and US legislation not only for what concerns insider trading but also for market abuse or market manipulation. In 2000, the UK Parliament promulgated the Financial Services and Markets Act 2000[28] which includes norms regarding the discipline of market abuse and civil offence for insider dealing. This Act highlighted three main categories for market abuse offence: misuse of information; create false\misleading impressions; market distortion. The regulatory discipline of the market abuse or manipulation was emanated not only with the objective to protect legally privileged information belonging to issuers of securities against abusive behaviours by insiders and related third parties, but also, and maybe this is the first objective, to defuse situations and circumstances that could undermine market confidence and equilibrium, including its systemic stability. Moreover, in order to better protect the market system, the market abuse offence was promulgated to enhance investor protection by prohibiting any individual from misusing information or create false "rumors" in the market. In contrast to the criminal offence of insider dealing discussed above, the statutory corpus of laws creating the market abuse offence covers behaviour and specific situations both in the market bot outside the market, including standard practice of trading activity and the action of disseminating false information (fake news nowadays).

[26] Criminal Justice Act, 1993. UK Public General Acts, 1993 c. 36 – SCHEDULE 2
[27] Directive 2003/6/EC of the European Parliament and of the Council, 28 January 2003, on insider dealing and market manipulation (market abuse) (repealed)
[28] Financial Services and Markets Act, 2000. UK Public General Acts, 2000 c. 8

In the early 2000s, just as every single Member State of the European Union had adapt its national legislation on the basis of the general directives issued by the European Parliament, also the United Kingdom had therefore modelled its current discipline of market abuse-manipulation in reference to the EU Market Abuse Directive 2003[29]. The new directive had therefore extended the three 1993-original market abuse categories to seven groups of behaviours very similar to the European Parliament outlines[30]:

1. *Insider dealing*
2. *Improper disclosure of inside information*
3. *Misuse of relevant information [...]*
4. *Manipulating transactions in the relevant market [...]*
5. *Manipulating devices*
6. *Information dissemination that gives or is likely to give a false or misleading impression*
7. *Misleading behaviour or distortion of the market where the behaviour falls below the standard of behaviour reasonably expected by a regular user of the market or an alleged abused [...]*

In general speaking, in European Union the Insider Dealing and Market Manipulation Directive had defined insider trading\dealing as a form of market abuse, more precisely the first form of behaviour that constitute market abuse, that can constitute civil and criminal offence. Even if could be misunderstood in the first place, the main scope of this discipline is to extend the personal liability for primary-standard insiders through the exclusion of the fundamental requirement of the knowledge of the material non-public information for criminal or civil liability to be imposed. It follows that, UE Directive recognized the reality of the market world, i.e., that primary-standard insiders could have access or may have the possibility to become in possession of insider information on a daily basis and are objectively aware of the privileged and confidential nature of this kind on information obtained. Moreover, it is interesting to observe that in Article 2[31] the Directive adopted an information relationship requirement to define the connection with the so-called secondary insiders. This requirement gave us the strictly connection in defining insiders, both primary and secondary,

[29] Directive 2003/6/EC of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market absue)

[30] The Financial Services and Markets Act 2000 (Market Abuse). UK Statutory Instrument, 2005 N. 381 – Schedule 2, paragraph 1, § 118 (2) – (8) personally revision

[31] Directive 2003/6/EC, Article 2. EC Market Abuse Directive 2003

anyone who possesses inside information with full knowledge. The term "insider" was then applied to any person who had inside information as a result of his membership of the administrative or management bodies of an issuer of qualifying investments, or moreover as a result of his holding in the capital of that issuer or obtained by other means.

1.5. Insider trading in UE

1.5.1. Origins of insider trading in UE

The European legislation about insider trading was born in November 1966 at the European Commission thanks to the report of a group of expert[32] which objective was to put the attention of the Member States on the necessity to the development of a European Capital Market new legal framework. For the first time in the history of the European Union, this document pointed the magnifying glass on insider trading, viewed like a technical problem related specifically to directors or executives dealing in shares of their company. The next step in Europe was in 1989 when the Council promulgated a directive[33] with the scope of coordinating the heterogeneity of the insider trading system in all the Member States (for example UK regime was very different with respect to the German one). Later on in 2003, the European Parliament enacted the Directive 2003/6/EC[34] which includes insider trading and, for the first time, market manipulation\abuse, the two most fundamental threats to control the development of capital markets. The last step in chronologically order was the new proposals published in 2011 by the European Commission both for directives both regulations to update its legal system on insider trading\dealing and market abuse\manipulation.

1.5.2. European Directives on National Member States laws

[32] Segre, Claudio. 1966. The development of a European capital market. Report of a group of experts appointed by the EEC Commission. November 1966. EU Commission – Working Document

[33] Council Directive 89/592 EEC of 13 November 1989 coordinating regulations on insider dealing, OJ L 334, 18.11.1989, p. 30-32 (ES, DA, DE, EL, EN, FR, IT, NL, PT)

[34] Directive 2003/6/EC, January 28, 2003 on insider trading and market manipulation (market abuse)

Today, European corpus of law on insider trading consists of the Market Abuse Directive 2003, the milestone of the entire regulatory regime, and two auxiliary directives: the Commission Directive 2003/124/EC of December 22,2033 and the Commission Directive 2004/72/EC of April 29, 2004. These two auxiliary directives are two expansions of the 2003 Directive and are in addition to the original Act and combined together gave us the general inputs for the National statutory regime of every single Member States. The choice to use directives rather than regulations granted a sort of discretion as to the choice of form and methods employed by the national organisms and authorities in transposing them into national law. In addition, the European Court of Justice has added to the effectiveness of directives by recognizing a principle of homogeneity and harmonious interpretation which requires unequivocally the national Courts to interpret any relevant national regime in the light of the European one.

The Market Abuse Directive applies to issuers of financial instruments like securities, futures, swaps, options and derivatives if they are either admitted to trading on a regulated market in at least one Member State or their value is affected by financial instruments of this type. This directive stated the definition of inside information in Europe[35]:

For the purpose of the Market Abuse Directive, inside information shall mean information of a precise nature which has not been made public, relating, directly or indirectly, to one or more issuers of financial instruments or to one or more financial instruments and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivatives financial instruments.

In Article 2 of the Directive, we found some definition of insiders, i.e. individuals who are in possession of inside information and are addressed of the law prohibitions. The document covers classic traditional insiders such corporate officers, directors, certain employees, shareholders and individuals who gain inside information through illegal behaviours. If we think of US regime, UE provisions seem to be broader than its overseas equivalent as far as shareholders are concerned. In details, the Security Exchange Act applies only to shareholders owning more than 10 percent of company's stock while UE directives refer to any person who possesses inside information thanks to his holding in the capital of the issuer. There is instead an equivalence for what regards "constructive insiders" or insiders on the basis of a non-traditional relation because we found this kind of insiders under US law and similarly in UE

[35] Article 1, Directive 2003/6/EC

regime if they have access to information in a professional context[36]. Moreover, Article 4 of the 2003 UE Directive extends insider trading prohibitions far beyond the scope of US regime to the secondary insiders, i.e., individuals in possession of inside information while they know, or ought to have known, that it is inside information.

1.5.3. Tipping and duty to disclose

Like US legislation, European Directives prohibitions could be divided into two main categories of trading and tipping. The normative structure of the practice of trading in conditions of inside information obtained is strictly in connection with the US laws, while the rules applied on the practice of the tipping are rather broad and without restriction with respect to the equivalent US misappropriation theory. We could find another parallel between the Market Abuse Directive and the SEC's practice of Rule 10b-5 for which an insider purchasing or selling a security on the basis of a contract which was concluded before the person possessed inside information does not violate insider trading prohibitions. The Article 3 of the 2003 Directive states the standard tipping situations for whom in insider trading if there are any disclosure of inside information to other persons unless such disclosure occurred in a professional situation, similar to US regime.

Therefore, it is clear that the presence of inside information has two legal consequences, the prohibition of insider trading transactions and the duty to disclose to the market. This disclosure duty creates a substantial difference between European system and US law, which did not recognize a general duty to disclose inside information under Rule 10b-5. In details, the Article 6 of the Market Abuse Directive obliged individuals to publicly inform the market of inside information if these conditions are met: he issues financial instruments; the inside information directly concerns the issuer; there is no permission to delay disclosure.

1.6. Conclusions

There are no doubts that insider trading legislation showed a pronounced influence of US regime on the European Directives, in particular with regard to the integration of the overseas debate on possession or use, other tests like probability and total information or reasonable investor term serving as guideline for assessing materiality of inside information. Maybe the most evident difference is the underlying policy reasons between US and UE lawmakers. For

[36] Market Abuse Directive Art. 2 para. 1 sub- para. 2(c)

example, European directives did not subscribe to any kind of misappropriation theories, but it proscribes insider trading ground of market integrity and fairness.

The influence of US law is considerably stronger on a technical level rather than on a policy statutory level. As seen before, US lawmakers rely on misappropriation theory, while European Council try to control insider trading conducts from the perspective of protect market integrity and stability to individual investors. We could say that we have two different point of views and perspective because the US statutory regime monitor nowadays the treatment of very similar issues under a substantial different policy like UE ones. For example, this is true for what concerns the objective of insider trading prohibitions and the qualification of non-traditional insiders. On the other hand, it is interesting to highlight how European lawyers transplant legal UE Directives arguments into National Member States regime. US law's scope of insider trading and market abuse prohibition is much narrower than that of European law and do not connect reporting requirements with the possession of inside material. If we try to put US and UE in a parallel line, we have the situation for which whenever findings on US research tend towards an expansion of the scope of insider trading law within the framework of Section 10 (b) and its Rule 10b-5, the effect is objectively stronger when applying closer arguments to the European context.

In order to draw a general conclusion about the regulation of insider trading, insider dealing, market abuse and market manipulation, as it emerges from the recent literature concerning both the US, Chinese and European regulatory systems, it is undoubtedly worth nothing that the judicial architecture will always continue in the future, as we have seen in the past, to raise questions and even inconsistencies in specific cases that will be faced with respect to other criminal conduct. This is due to the fact that the complexity of the market system and the sophistication of the financial markets, within which the law must operate through its multiple judicial bodies and authorities (recall the SEC and the Supreme Court in US, or the CRCS in China as examples) in practice and in cases that the reality presents day by day, reinforce the judicial difficulties of legal practices that officials who seek to administer and enforce the theoretical law must face.

Expanding the vision on the control system of information abuse and market abuse, it is clear that those two crimes have much in common with the application of the laws regarding, for example, money laundering or corruption crimes, nevertheless the complex development of legislation and the constant updating of a supporting regulatory framework will always prove to be a sensitive and difficult international issue to address. Despite this general underlying complexity, the effectiveness of the anti-insider and anti-market abuse rules in recent years

seems to have become increasingly efficient both on a global level thanks also to the several investigations by the competent bodies. In the financial sector, there is no country in the world that had not recognized at the legislative and political level the fact that the control over the abuse of information and the market is an extremely significant issue, maybe the most significant, when it comes to being able to safeguard transparency and preserve investor confidence in the integrity of the markets.

Regardless of whether it is the application of civil law or criminal law depending on the country system, as we have seen within this chapter, there is no doubt that the control over these abuses is of public utility and that it will have to be in the future always a central theme for safeguarding the entire economy of the countries.

2. Chapter 2 – Netflix Insiders and Elon Musk cases

2.1. Introduction

In Chapter 1, our analysis has highlighted the evolution of the regulation about "insider trading" or "insider dealing – market abuse" through different geographical areas – Europe, United States, China – and different periods of time. At the end of the Chapter 1, our journey around the world oh the insider trading brings us to a preliminary final partial conclusion: in the economic global system there is a kind of general guideline about its regulation, but still there are some "grey zones" that leaves an ambiguous empty space where potential insider traders could stay without being out of-the-regulation.

In this Chapter, we want to focus our attention on two famous and current examples of situations where potential insider trading could be detected or fall to be detected. Going through those two litigations our objective is to state if the regulation was violated, how the authority has acted in order to detect the violation, what kind of sanction was inflicted to the insider traders and if this litigation (and its consequences) could be dealt with the same modalities in the other areas referred to Chapter 1.

The first litigation we will analyse concerns the scandal of Netflix's corporate insider treaders, that was brought to light by the American press in the early 2021. This case has had, and continues to have, a notable resonance in the world of insider trading and the abuse of non-public material to gain large amount of US dollar trading with securities. We will focus on how Netflix' internal company regulation could create some opportunities for its employee to anticipate financial market in trading with securities with respect to all other investors and how some of Netflix employee have benefited from their insider position. After that, we will analyse how this case have been treated by US regulation and we will compare it with respect to EU insider trading regulations and finally with the Chinese ones.

In the second part of this Chapter, we will focus our attention on another complex and famous case that will allow us to wonder and reflect on how statements and publications on social media (like Twitter) could move suddenly market prices of stock securities and how market abuse regulation should protect investors and stakeholders. This is the litigation between the Securities and Exchange Commission and Elon Musk – TESLA: firstly, the accusation of insider trading by Elon Musk and his brother with TESLA securities, secondly the accusation of market manipulation by Elon Musk through his activity on Twitter.

2.2. Netflix case

The 18th of August 2021, Erin E. Schneider – director of the San Francisco regional office of the SEC – announced that the authorities had accused[37] one Netflix employee, and his close collaborators, to have elaborated a millenary fraudulent scheme in order to gain profits from precious company's non-public information. Securities and Exchange Commission explained that this criminal scheme was based on non-public rate of growth of Netflix monthly new subscribers. This fundamental information was the centre of the financial decisions of the defendants of the SEC' action to trade the multinational of the streaming shares ahead of its public earnings announcements. According to the compliant, Sung Mo Jun – the main architect of the whole illegal scheme – while he was working as a software engineer at Netflix from 2016 to 2017, had frequently informed his brother and a close friend about this rate of new subscriber's growth. The latter, thanks to Song Mo Jun, had benefited from it to trade before subsequently quarterly Netflix earnings announcements.

The summary of the action concerns a three-years criminal scheme from which insiders have gains a sum of circa three million illicit profits through the trading on Netflix securities thanks to non-public material. How everyone already known, Netflix, Inc. is the first company in terms of turnover and overall importance in the field of online streaming through its app or web site of TV series, films, cartoons, and documentaries. Netflix common stocks are registered with the Commission pursuant to 12(b) section of the US Exchange Act, listed on NASDAQ under "NFLX". Some relevant facts that SEC highlighted in its action cover a period of time which starts from July 2016 and finishes in July 2019. The entire compliant is based on insider trading in Netflix securities in advance of thirteen separate quarterly earnings announcements of the company.

2.2.1. SEC vs. Netflix Insiders

In details, there was a total of five individuals that were been defined as "insiders" and had violated the Section 15 of the Exchange Act: Sung Mo Jun, Joon Mo Jun, Junwoo Chon, Ayden Lee and Jae Hyeon Bae. In this case, it is very important to highlight every single relation within these persons to detect and to discover the criminal behaviour of them.

[37] SEC v. Sung Mo Jun, Joon Mo Jun, Junwoo Chon, Ayden Lee and Jae Hyeon Bae, August 18, 2021

In particular, the SEC put its magnifying glass on Sung Mo Jun, who was the main architect of the entire insider trading ring both when he was working physically at Netflix and after he had left his job[38]. He was employed as a software engineer at the company from December 2013 to February 2017. The second defendant in this compliant is Joon Mo Jun, Sung Mo Jun's brother, and the third one is him close friend Junwoo Chon. Then we have the fourth participant of this "insider ring", Ayden Lee. He was a software engineer at Netflix from May 2016 to February 2021 and he met Sung Mo Jun at the first job interview for an open position in his role. After getting the hiring, Lee worked with him from May 2016 to February 2017 and in this period Sung Mo Jun became his mentor. Finally, we have the last of the list Jae Hyeon Bae, data software engineer for Netflix from July 2012 to April 2015 and then from June 2017 to July 2019. In his first period at the company, he met Sung Mo Jun and became his close friend while they were working in the same team group.

To better understand the architecture of insider trading operations carried out by the "insider ring", it is useful to underline some data and personal details[39] of the subjects in question:

- Sung Mo "Jay" Jun (referred to as Mr. Sung for further remarks), 49 years old. He was employed as a software engineer at Netflix from December 2013 to February 2017, then starting from 2018, as a senior engineer at an IT multinational outside US and finally, from 2019 to 2020 at a Seattle company as a senior software engineer
- Joon Mo Jun (referred to as Mr. Joon for later remarks), 45 years old, brother of Mr. Sung
- Junwoo Chon (referred to as Mr Joon for later remarks), 45 years old, brother of Mr. Sung
- Junwoo Chon (referred to as Mr. Junwoo for future remarks), 49 years old, a very close friend of Mr. Sung since his teenage years, the two have known each other from about 20 years
- Ayden Lee (referred to as Mr. Lee for further remarks), 33 years old, was employed as a computer programmer at Netflix from May 2016 to February 2021. Mr. Lee first met Mr. Sung during the initial job interview and worked closely with him from May 2016 to February 2017. It can be said that Mr. Sung was a real mentor for Mr. Lee during his work experience in Netflix
- Jae Hyeon Bae (referred to as Mr. Bae for future remarks), 42 years old, was employed at Netflix as a software and data engineer in two distinct periods of time:

[38] Summary of the Action SEC V. Sung Mo Jun et al. (No. 2:21-cv-1108)

[39] This part is taken from the "Defendants" at Compliant SEC v. Sung Mo Jun et al. (No. 2:21-cv-1108)

from July 2012 to April 2015 and subsequently from June 2017 and July 2019. Mr. Bae also worked closely with Mr. Sung during his early term as they were placed in the same engineering group and became then friends

Our analysis could reassume and summarize the entire action of the United States District Court – Seattle Division of the Western District of Washington versus these five defendants in some relevant facts. Firstly, Sung Mo Jun was the starting point of the entire crime when he was working at Netflix offices, both when he left his position at the company. Authority obtained the proof that he accessed material non-public information regarding Netflix new subscribers' growth. As everyone knows, one of the most important key-drivers of the market value of Netflix's securities is the rate of growth of monthly new active subscriptions on the platform. In the same way, that rate is the fundamental core business key-driver of the subscription-based online streaming company's revenue and global success. Thanks to this inside information, Sun Mo Jun tipped his brother Joon Mo Jun and his close friend Junwoo Chon in order to get profits from the trading on NFLX securities in advance of four consecutive quarterly earnings announcements (July 2016 – July 2017). Sung Mo Jun received about 60.000 US dollars from his friend's profit due to his information leakage[40].

As said previously, Sung had a central role in all this action even when he left his position as a software engineer. In particular, he was able to obtain confidential subscribers' information from another Netflix employee, Ayden Lee. As explained before, Lee worked with him in close contact in daily tasks team work and became his friend. In the period June 2017 – July 2019, Lee frequently tipped Sung, in the same way the latter did with his brother, who traded ahead the related quarterly earnings announcements. At the same time, Sung tipped Joon Jun and Chon to trade in Netflix securities, too.

Subsequently, a former colleague of Sung Mo Jun, Jae Hyeon Bae, created a secret group "messaging channel"[41] with Sung, Joon Jun and Chon with the objective to share with them stock trading tips. Thanks to this tipping-channel scheme, Sung, Joon and Chon netted over 3.1 million in illicit profit from trading Netflix securities and derivatives based on insider non-public information provided by Lee and Bae from July 2016 to July 2019, according to Seattle District investigations.

To detect the insiders' violation, the Court had to demonstrate that the rate of subscribers' growth of the company entered the field of non-public material information, that is every kind of information that can moves, or potentially could moves, market price of NFLX securities if

[40] Summary of the Action SEC V. Sung Mo Jun et al. (No. 2:21-cv-1108)

[41] This term was used by the SEC at line 18 of the ibidem Action

it could be available for all investors. Moreover, Netflix's core business is the streaming for a monthly fee of movies, tv shows, documentaries and similar, therefore its revenues' growth is in strictly exponential correlation to its new customers' performance. The subscriber's performance number is material information because the company makes it publicly available in its quarterly earnings releases.

Now we must wonder how it could be possible that such fundamental information could have been reached by the accused. As already Netflix makes visible through its web site, monthly subscribers' number is made available by the company to its employee through its intranet on an ongoing basis. Every single employee must know that Netflix considers this data as an internal confidential information according to the policy statement in the part regarding insider trading articles[42]. Before having obtained the working position at the company, every employee must read and sign this internal policy which prohibits them to trade in Netflix securities based upon material non-public information. Furthermore, the policy prohibits from making recommendations or expressing advice about trading based on such information.

The choice to inform its employee about the new subscribers to the platform reflect the company's vision of make aware its human resources about their efforts in every level of employment in order to create a stimulating and satisfying working habit in which they could see personally the results achieved. At the same time, Netflix try to prevent illicit behaviours that could emerge in relation to its choice with its Insider Trading Policy.

As we have just observed, the are no doubts that the rate of growth of new subscribers on Netflix platform is clearly material non-public information. In the same way, it is evident that Sung Mo Jun was aware of the company's insider trading policy due to the fact that if he didn't sign that document, he wouldn't be hired as a software engineer at Netflix.

The fact that Netflix subscribers' information is recognized as non-public material by the company itself and also by the Court brings us directly to the first factual allegation by the SEC: each individual who had gained or profited through the knowledge of this kind of confidential information, is subject to the rule 10-5 (b) about insider trading[43].

The action against Netflix insiders continues with some other relevant facts like the proof that Sung Mo Jun, in his first working period at the company, had accessed this kind of confidential material from July 2016 to February 2017. That number of new monthly subscribers would be published only during Netflix quarterly earnings announcement to

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[42] Netflix Insider Trading Policy Act, available at https://ir.netflix.net/governance/governance-docs/default.aspx
[43] Factual Allegations SEC V. Sung Mo Jun et al. (No. 2:21-cv-1108)

market investors. During this period of time, Sung Mo Jun must know that it was prohibited to use this kind of information in such a way to tip other individual and make profit by the trading on Netflix securities and derivatives.

The Court accused Sung Mo Jun to had violated his obligations to the Company because he had recommended or has expressed personal advice to Joon Jun and Chon in the period July 2016 – February 2017. Sung did it in order to have in return a personal gain urging Joon and Chon to trade in advance with respect to Netflix earning announcements in its securities. Moreover, the District had accused Sung to be got paid in cash for subscriber's confidential information from Joon and Chon after they had profited with such a trading strategy.

On the other hand, both Joon and Chon are partners in crime together with Sung because they knew that their friend\colleague could be probably had supplied information that shouldn't be clearly expressed outside Netflix company. Anyway, they did not inquire if they would be liable to crime in using such material non-public and there are few probabilities that they did not have the way to access to insider trading policy. In fact, they could be aware of their positions simply by surf Netflix's website to the section company policy. In addition, Joon and Chon have repeatedly traded in this way for a long time without having informed about the possible future consequences of their behaviour and always in advance to company earnings announcement for July 2016, October 2016, January 2017 and April 2017.

Another interesting analysis of the Court had brought to light some strange market orders placed by Joon and Chon. Ther results of the investigation are another proof of insider trading because during the period of time explained above Joon and Chon had placed trades minutes apart for identical Netflix option contracts, specially put options and call options contracts[44].

Although Sung Mo Jun had terminated his employment contract with Netflix in February 2017, beyond having violated the company insider trading policy with his recommendations and tipping behaviour with Joon and Chon, he furthermore had personally traded Netflix securities in advance to April 2017's public earnings announcement and so he had also violated the articles regarding employments insider trading in company securities.

The Security Exchange Commission also managed to find sufficient evidence to establish that Sung Mo Jun, Joon Jun and Chon managed to exchange information with each other regarding their trading operations in financial instruments deriving from the Netflix stock through a complicated computer application of encryption of sentences and terms in code with the aim of avoiding being tracked down and therefore subsequently sanctioned. As mentioned

[44] Factual Allegations SEC V. Sung Mo Jun et al. (No. 2:21-cv-1108)

at the beginning of the paragraph, the individuals in question, being brilliant computer engineers and expert programmers (an inference deriving from the fact that if this were not the case, they would never have passed Netflix's complex job selections based on high standards of computer skills and code programming), have managed over the years to exploit their brilliant skills to be able to derive a benefit in terms of insider trading. Despite this, the lengthy investigations by the SEC have led to some objective results: thanks to this conduct, Mr. Joon Jun obtained approximately 215.000 dollars in profit while his partner in crime Mr. Chon approximately 521.000 dollars[45]. Those profits became illegal profits because they have traded after having obtained insider information in advance of Netflix's quarterly earnings announcements of July 2016, October 2016, January 2017 and April 2017 based on material non-public information of the company growth of subscribers. In addition, Mr. Chon rewarded partner Sung Mo Jun for the transmitted information 60.000[46] dollars, which increased the latter's illicit profit to 275.000 dollars as the sum of his primary insider trading personal activity and the practice of the tipping.

Another key element of the sentence concerns the role of Mr. Lee, who as mentioned at the beginning, first met Mr. Sung Mo Jun during his job interviews for an open position as a computer engineer at Netflix in 2016 and secondarily immediately after he was hired in May of the same year as, by company policy, Mr. Lee was placed in the same working group as Mr. Sung. As mentioned above, one of the fundamental recruitment requirements to be able to become part of the Netflix Inc.'s world on a professional level is the acknowledgment of the company's Insider Trading Policy, complete with the original personal signature. As can be easily seen from its official website, Netflix has always been very clear about its corporate, ethical and motivational policies and every deed, document or regulation is easily available through its information channels (as well as being immediately presented and explained to all employees or internal and external collaborators at the same time as the hiring or stipulation of the professional\collaboration contract). Furthermore, as already was established at the time of the ancient Romans through the Senate of the Republic *"ignorantia legis non excusat"*, i.e. well-known expression in the legal field and the maximum synthesis of the legal concept valid worldwide starting from the ancient Roman law of the presumption of knowledge of the law, whose literal meaning is that ignorance of the law does not exonerate individuals from applying it if it is not respected, in the same way Mr. Lee must have been objectively aware of at least the company's internal regulation on insider trading as he had been obliged to read it with the countersignature of the deed. In addition to this, we have already observed that

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[45] Estimates took from Factual Allegations SEC v. Sung Mo Jun et al. (No. 2:21-cv-1108), co. 23, line 5, pag. 6
[46] Ibidem at line 8, pag. 6

Netflix, as an internal motivational policy, openly previews data on the growth of new subscriptions and users registered on the digital platform on a daily or weekly basis to make its employees or collaborators aware that the efforts made during the planning and programming phase have a real impact on the company performance (almost a sort of "award" or recognition to one's staff which leads to a continuous stimulus to improve more and more in one's work).

There is therefore no doubt that this type of data disclosed in advance of the public is objectively material non-public information that Mr. Lee could under no circumstances have used for external trading or tipping at least until the exact moment of the publication date of such data during the company's quarterly earnings announcements to the market as required by law for listed companies (also remember the principle of public disclosure). On the basis of the aforementioned observations, the SEC refers to these general conditions directly in the original document always within the "Factual Allegations".

The document then continues chronologically arriving at February 2017, the moment in which Mr. Sung decides to leave his job position at Netflix to find work elsewhere. Although he was no longer physically present at the corporate offices, he repeatedly and frequently asked Mr. Lee to continue to provide him with the same confidential information on the results of the number of new subscribers to the digital platform given that the latter, still being a computer programmer Netflix, had constant access to this type of data. As explained before, the relationship between these two individuals can be inserted within that set of student-teacher\mentor relationship for which the student (Mr. Lee in this case) sees his mentor (Mr. Sung) as a figure important to respect and imitate on a professional level as he tries to learn as much as possible from the master to aspire to reach his levels. It is useful to underline that Mr. Lee arrived very young and with little experience at the initial interview with Netflix through Mr. Sung, who on the contrary had already accumulated such professional experience and prestige as to be appointed by the same company to scrutinize the various candidates from the neo-programmers to include them in the IT staff. It can be said that Mr. Lee learned the entire profession at Netflix through Mr. Sung, who, given his more adult age, "took him under his wing" in the computer engineering team to become his mentor and model to follow. Mr. Sung therefore exploited and took advantage of his position within this relationship to take advantage of it and trade with guaranteed and safe illicit profit. On the other hand, Mr. Lee did not have the courage to refuse his requests and indeed perhaps he even acted with full awareness of the fact that his conduct was in all respects punishable as he knew that the information he was providing was objectively confidential and undisclosed, almost as if it

were a gift or the right reward absolutely due to his mentor who had made him grow and reach his dream job at Netflix. We could be sure of this thanks to the fact that the SEC itself has not found any kind of back payment or reward from Mr. Sung to Mr. Lee for the repeated and constant disclosures of the data from June 2017 to July 2019, as if it were a voluntary and completely free tipping practice of recognition to his master[47]. Nonetheless, Mr. Lee was fully aware of the fact that Mr. Sung would obviously have used his information to generate enormous illicit profits governed by the insider trading discipline primarily of Netflix, and above all of the American legislature.

Moreover, during the aforementioned period of time, Mr. Sung in turn reported the same non-public Netflix information to Joon Jun and Chon thereby in turn committing tipping for the purpose of trading in Netflix securities. Again "ignorantia legis non excusat" as Mr. Joon and Mr. Chon must have known, or were reckless in not knowing, that Mr. Sung was gathering that information from a company insider source as he was not working more at Netflix. Here therefore, the so-called "insiders ring" begins to take shape thanks to the central link of the entire structure to be depicted in the person of Sung Mo Jun as he assumed the role of intermediary between his personal internal source and his partners. From the careful analysis of the SEC survey, it therefore emerged that between June 2017 and July 2019, Mr. Sung managed to obtain a profit of approximately 453.000 dollars, in turn Mr. Joon managed to secure approximately 813.000 dollars of profits and finally Mr. Junwoo approximately 1.100.000 dollars thanks to the trading in advance of nine consecutive Netflix earnings announcements[48].

Continuing with the analysis of the SEC compliant we arrive at the final closure of the insiders' ring through the entry into play of the last convict: Mr. Bae. However, it is necessary, also in this case, to place our attention initially, once again, on Mr. Sung's sphere of knowledge and relationships. While he was still employed at Netflix, in addition to becoming Mr. Lee's mentor, Mr. Sung's team also included Mr. Bae, another software development engineer of the online steaming platform. The SEC investigation found enough evidence to establish that the relationship between the two colleagues was very strong on a professional\work level both on a friendship level outside of working hours. We certainly cannot speak of a brotherly or student-mentor relationship as in the case of Mr. Lee, but there is no doubt that the figure of Mr. Sung within his team of IT engineers stood out for his skills, temperament and leadership so much as to succeed to establish a relationship of friendship

[47] Ibidem at lines 23-28, pag. 6
[48] Ibidem at lines 11-13, pag. 7

with all his colleagues, of which the strongest one was precisely in relation to Mr. Bae. As previously noted, therefore, this last individual also had the opportunity to constantly observe the performance of the growth rate of Netflix's new subscribers as an employee of the company (remember the previous paragraph on the motivational policy of Netflix, Inc.).

In February 2018, thanks to his strong friendship with Mr. Sung and also to direct knowledge of Mr. Lee, Mr. Bae joined the private messaging select group named by the SEC "Messaging Channel" (as mentioned in the introduction). This coded group also had an actual name "Range Against the Market"[49], hosted on a popular business communication platform, which also included the other conviction insiders, i.e., Mr. Sung, Mr. Joon and Mr. Chon. Nowadays, these types of social groups are very frequent especially through the Whatsapp and Telegram channel\app if we think of the world of cryptocurrencies or network marketing through information and training on trading of any type. In this case, however, the private messaging group was used as a point of references for warnings, indications, investment advice and useful tips in terms of securities trading and Mr. Bae, the least experienced among the participants in the inner circle, was just joined the channel with the aim of being able to obtain some useful tips or information that could have helped him to make safe money through transactions in securities and financial instruments.

The Factual Allegations proceeded to examine a precise moment inside the messaging group when Netflix's business and financial performance began to be discussed within a message sent while discussing what might be the best current investments to make trading at the time. In particular, it was highlighted that Mr. Joon used this channel just a few days before the public Netflix quarterly earnings announcement of July 2019 to indirectly ask Mr. Bae for an opinion on the performance of the company where he was employed, knowing that he had access to data on the performance of new underwriters. Mr. Bae therefore, after realizing that it was clearly an illicit request to be able to take advantage of his position as an insider source, without giving precise indications on specific data, replied that he would have sold Netflix shares to obtain a certain profit. The SEC highlighted this passage between the various messages of the channel as Mr. Bae was aware of the real performances that would be announced shortly thereafter by Netflix and gave the advice to sell precisely because at the moment in the market the analysts financers confidentiality predicted that the results would be growing while Mr. Bae was already aware of the fact that the earning announcements of July 2019 would be below expectations (and therefore the share price would certainly fall).

[49] Ibidem at co. 30, lines 25-26

Also in this case, however, we faced with a situation of "free tipping", specifically by Mr. Bae towards Mr. Joon as the investigations have not found any type of payment\reward towards Mr. Bae for the recommendation of inside information in the group. This free favour was provided precisely because, being the "latest addition" to the private channel, Mr. Bae hoped in this way to be rewarded with further recommendations or future advice on other financial instruments and stocks from the other partners in the channel, much more experienced and with potential information ahead of the market.

Although all participants in the group were fully aware that Mr. Bae was employed by Netflix and that trading based on his information provided regarding the growth rate of the number of subscribers would be punishable by the offense of insider trading, in addition with the help of Mr. Sung too who in the meantime had asked his partner Mr. Lee at the same time for more specific data, Mr. Joon illegally traded Netflix securities in advance of its July 2019 earnings announcement generating profit of 72.875 dollars[50]. In this case we are therefore faced with a practice of "double-tipping" with no monetary reward in return, thanks to the general advice provided by the insider Mr. Bae in addition to the recommendation provided by Mr. Sung through the insider Mr. Lee on more specific data on confidential material non-public information.

2.2.2. Netflix Insider Trading Policy

In this part of the chapter, we will try to analyse Netflix, Inc.'s corporate policy on insider trading to deepen and define what exactly are the prohibited behaviours and the actions condemnable for criminal conduct. As noted above, Netflix has a legal agreement with its employees and corporate members regarding its obligations and prohibitions with respect to trading and inside information that continues until the end of the direct employment or contractual relationship with Netflix company. In addition, to being viewed and signed at the time of hiring, this agreement is also available for viewing by the public through its official website in the part reserved for investors "Environmental, Social & Governance" section in the "Governal Docs" part. In this part of the site, we therefore find the document relating to the trading policy to which this chapter refers, i.e., Insider Trading Policy 20220228, version date February 28, 2022.

This document begins by immediately clarifying the fact that the company wants to be able to play an active role in preventing possible violations by its employees and directors regarding

[50] Ibidem at page 8, line 20

the practice of insider trading and abuse of privileged information. The main intent of this policy is therefore clearly to establish that Netflix, Inc. opposes any abuse of material non-public information in the trading of securities and therefore undertakes to outline operational procedures to be followed in order to prevent trading based on material non-public information regarding the company and its subsidiaries. It is also useful to underline that it is expressly written that the company discourages certain types of trading in its securities by its officers and employees which could potentially be against the interest of the shareholders. With the term "officer", Netflix intends to use the legal definition expressed under Rule 16a-1 (f) of the Securities and Exchange Act 1934:

Directors, officers, and principal stockholder required to file –

Every person who is directly or indirectly the beneficial owner of more than 10 percent of any class of any equity security (other than an exempted security) which is registered pursuant to Section 12, or who is a director or an officer of the issuer of such security, shall file the statements required by this subsection with the Commission.

Netflix also discloses that this act is valid both for its officers, directors, employees, consultants or contractors and for its immediate family members or members of their households, who are all considered insiders at the same level. In addition to therefore establishing which types of people this policy refers to, Netflix also clearly expresses which type of transactions it refers to: i.e., all transactions in Netflix securities like common stocks, options, securities issued by the company, preferred stocks, warrants, convertible debentures, derivatives securities and publicly traded options issued by Netflix.

Subsequently, it is established what transactions Netflix insiders actually prohibit, such as the purchase or sale of the company's securities (including any type of offer to buy or sell) during any period commencing on the date the insider obtains possession of material non-public information concerning Netflix or its subsidiaries and ends exactly on the first available trading day following the date of the public disclosure of that type of information. It is possible to observe a clear example precisely in the SEC compliant analysed above by taking the number of new Netflix subscribers as a reference for material non-public information and as public disclosure date the quarterly earnings announcements which include precisely that type of information.

Proceeding in the prohibited transactions section, it is expressly forbidden for insiders to carry out tipping activities, i.e. disclose material non-public information of the company or its subsidiaries to persons who could take advantage of such information to obtain a profit by trading in the company's securities and, in any case, it is also prohibited to express opinions or make recommendations based on this material as could be used to obtain illicit profits by trading in financial instruments related to Netflix's securities. Furthermore, the general prohibition against undertaking transactions that could involve purchases or sales of other companies' securities is also defined if you are in possession of information relating to these companies obtained thanks to previous work experience with them or thanks to services or consultancy carried out with them, as Netflix has a duty of trust and confidence in relation to information relating to these companies through its employees or directors.

It is further specified that, unless there is a disclosed participation in the Netflix stock options program, no director or officer may engage in transactions involving any type of hedging or derivatives activity of Netflix securities including trading in futures, derivatives, exchange trade options, puts, calls, collars, forward sale contracts, equity swaps, exchange funds or other instruments designed to hedge relating to its securities.

The document proceeds with the description of "problematic transactions" and the definition of a very important part of the entire corporate policy. It is a question of establishing that although Netflix employees are not obliged (with the exception of officers) to submit to the previous section in which it was forbidden to use company securities as collateral for loans or in margin accounts or the whole issue relating to the hedging practice, Netflix strongly recommends to completely refrain from these types of transactions as such activities may result in transactions in Netflix securities occurring outside the "Operation Window" (to be defined later). Furthermore "limit orders with brokers should not extend beyond any Open Window and be cancellable upon an imposition of a black-out period"[51]. For all employees who find themselves in a trading position outside the Open Window, they must by statute adopt a trading plan defined through the standards imposed by Rule 10b-5 (1) of the Securities and Exchange Act 1934. That Rule established by the SEC in 2000, allows insiders of publicly-traded corporations to set up a trading plan for buying or selling stocks they own. Rule 10b-5 (1) permits major holders to buy or sell predetermined number of shares at a predetermined time and many corporates' executives used this Rule and its plan to avoid the accusations of insider trading. The SEC had always strong recommended that company like Netflix permit an executive to either adopt a trading plan under its Rule when they are

[51] Netflix Insider Trading Policy, 20220228, page 2 – Problematic Transactions

allowed to trade securities in parallel to their insider trading policy. Anyway, this Rule prohibits any insiders from changing or adopting a plan if they entered in possession of material non-public information. Following, a general overview and guidelines for establishing a legal trading plan[52]:

- The price and the amount must be specified, and dates of sales\purchase must be noted
- There must a be a formula or metrics criteria for determining the amount, price, and date
- The plan must give the broker the exclusive right to determine when to make sales\purchases as long as the broker is not in possession of material non-public information when the trades are being made

Netflix's Insider Trading Policy then proceeds to establish who are actually subject to the aforementioned possibility of trading during the Open Window. This possibility is therefore extended to all insiders (previously defined) with the exception of:

- *Non-salaried employees of the Company's DVD division*
- *Employees, contractors and consultants who are employed or retained through a director or indirect subsidiary of the Company that is specifically and solely engaged in the production of original content and not otherwise included as a matter of business practice in the distribution of corporate information about the Company and its financial performance, unless such person has been notified in writing by the Compliance Officer that the trading window applies to them*
- *Employees of subsidiaries that are not integrated into the Company's email system and who do not have access to member or consolidated financial data (for example, Scanline and Netflix Animation employees)*[53]

The Company therefore prohibits these individuals from buying, selling or effecting transactions in any stock or securities of Netflix or its subsidiaries outside the so-called trading window: "beginning at the open of market on the trading day following the date of public disclosure of the Company's financial results for a preceding calendar quarter of year

[52] Final Rule: Selective Disclosure and Insider Trading, Securities and Exchange Commission, 17 CFR Parts 240, 243 and 249, Release Nos. 33-7881, 34-43154, IC – 24599, File No. S7-31-99 , RIN 3235-AH82, Selective Disclosure and Insider Trading

[53] Netflix Insider Trading Policy, page 5, Attachment 1, Persons subject to trading window restrictions

and ending at the close of market on the 10th day of the second calendar month of the current calendar quarter”[54].

In addition to this time slot that Netflix makes available to its insiders, it is still possible, upon acceptance by the Compliant Officer, to authorize other time slots in addition to the trading window. In the same way, however, Netflix makes use of the possibility of unequivocally imposing special “black-out” periods during which everyone without distinction, or only certain types of individuals, is prohibited from carrying out trading operations even during the Open Window. In addition, for the Company’s added protection, if a special blackout period is imposed, the Company will notify affected persons that thereafter they should not engage in any transaction involving the purchase or sale of securities of Netflix and even the disclosure of this period of absence by these individuals to other employees or directors is prohibited.

It is then further highlighted, for maximum clarity and transparency, that in any case it is forbidden to carry out transactions (even in the Open Window) by all insiders who have come into possession of non-public material information. Moreover, after having defined the Open Window all the possible changes to this period of time in which insiders can carry out transactions, a sort of ad hoc regulation tailor-made for Netflix officers and directors is expressed.

In fact, it is established that they must compulsory, even if under an Open Window or additional pseudo-open windows regime, in the event that they wish to undertake trading initiatives of Netflix’s (or its subsidiaries) securities, submit an official request to the Compliance Officer. After this first contact, a pre-clearance can therefore be obtained to commence trading on the Company’s securities, nevertheless officers and directors must in any case comply with Section 16 of Security and Exchange Act of 1934 and its regulations regarding reporting obligations and disclosure and the related limitations about reporting obligations and limitations about the issue of short-swing transactions. Furthermore, Netflix, through its compliant office, makes available to its employees the possibility of being assisted in the compilation of the various documents to be presented in the event that an individual requests its personally.

To further clarify the section on trading plans based on Rule 10b5-1, the Company permits all directors, officers and employees to adopt trading plans in accordance with the specific Rule 10b5-1 (c) by the SEC and urges them to request specific information or assistance to its competent Compliance office in order not to be in the position of illegal conduct or not in

[54] Ibidem, The Company’s Trading Window

accordance with the law. In order to make clearer this part, we have to highlight what paragraph (c) of Rule 10b5-1[55] is:

Affirmative defenses. Subject to paragraph (c) of Section 10, a person's purchase or sale is not "on the basis of" material nonpublic information if the person making the purchase or sale demonstrates that:

A. *Before becoming aware of the information, the person had:*
   a. *Entered into a binding contract to purchase or sell the security,*
   b. *Instructed another person to purchase or sell security for the instructing person's account, or*
   c. *Adopted a written plan for trading securities*
B. *The contract, instruction, or plan described of this Section:*
   a. *Specified the amount of securities to be purchased or sold and the price at which and the date on which the securities were to be purchased or sold;*
   b. *Included a written formula or algorithm, or computer program, for determining the amount of securities to be purchased or sold and the price at which and the date on which the securities were to be purchased or sold; or*
   c. *Did not permit the person to exercise any subsequent influence over how, when, or whether to effect purchases or sales; provided, in addition, that any other person who, pursuant to the contract, instruction, or plan, did exercise such influence must not have been aware of the material nonpublic information when doing so*

As in any regulation or directive, also in this case exemptions from this policy are presented which can be summarized as follows: the exercise of stock options under Netflix's stock option plan with a cash payments of the exercise price (since the Company itself represents the counterpart in these type of transactions and their price is always fixed by the terms of the option agreement), and possible "bona fide" gifts of the securities of the company (given that a gift can be considered in good faith depending on the type of context, even here Netflix encourages consultation and assistance through the Compliance Officer in this case).

The policy continues with the section relating to the consequences of possible violations of the above statements, which are mainly divided into[56]:

[55] **§ 240.10b5-1 Trading "on the basis of" material nonpublic information in insider trading cases**
[56] Ibidem, Consequences for Violation

- Sanction by Netflix, Inc.: disciplinary action by Netflix which could include ineligibility for future participation in the Company's equity stock option and incentive plans or termination of employment
- Sanction by US federal and state securities laws: criminal and civil offence and penalties as well as imprisonment for engaging in transactions in Netflix's securities when they have knowledge of material non-public information
- Sanction by US federal and state securities laws: insiders may be liable for improper transactions by any individual to whom they have disclosed material non-public information regarding the Company or its subsidiaries, or to whom they have made recommendation\expressed opinions on the basis of such material (tipping practice)

In addition to outlining possible penalties that an insider could incur in the event of unlawful behaviour based on Netflix policy, the company then reiterates that each individual under contract to it or its subsidiaries has a personal individual responsibility respect to this statute and is therefore personally responsible for his trading conduct under the applicable federal laws in his jurisdiction. It useful to report the following advice highlighted by the company to its insiders precisely in the part dedicated to "individual responsibility"[57]: *trading in the Company's securities during the trading window should not be considered a "safe harbor", and all directors, officers and other persons should use good judgement at all times*. As if that were not already clear enough, Netflix expresses itself very clearly to its insiders to make them aware of their responsibilities and duties regarding insider trading precisely to safeguard their protection in the world of trading.

Moreover, we find the definition of the roles that are attributed to the Compliance Officer, the central figure of the whole policy both for the Netflix's General Counsel shall serve as the Insider Trading Compliance Officer and that his primary responsibilities and duties are to[58]:

- Pre-clearing transactions
- Assisting in the preparation and filling of Section 16 reports (Form 3, 4, 5) for Section 16 standard reporting persons
- Serving as the designated recipient at the company of copies of reports filed with the SEC by Section 16

[57] Ibidem, page 4 – Indivual Responsability
[58] Ibidem, Compliance Officer

- Periodically reminding to the designated reporting individuals regarding their obligations to report and quarterly reminders of the date designated for the trading open windows
- Circulating the insider trading policy to all employees on an annual basis
- Coordinating with Netflix counsel regarding compliance activity with respect to Rule 144 requirements and possible changing requirements and recommendations for compliance with insider trading laws

As can be observed, it certainly cannot be said that Netflix insiders are not accompanied at 360 degrees in the process of learning about the legislation on insider trading, nor that they are not assisted and helped with regards to the procedures to follow in order to avoid possible accusations.

In closing, the document also tries to give a general definition of "material non-public information" based on the general rule that this type of information must in some way refer to news that could be considered important by a rational investor during his investment decision in buying or selling securities of Netflix or its subsidiaries. In any case, it is expressly stated that since it is impossible to index all the possible categories of material non-public information (as we analysed in Chapter 1), it is always possible to obtain clarifications from the Compliance Officer.

2.2.3. Conclusions

As it was possible to deduce from the SEC indictment of Netflix insiders and from the company's Insider Trading Policy, objective conclusions can be drawn regarding the behaviour of the participants of the so-called "insider ring" with respect to both the federal law on insider trading but above all with respect to the policy. The creation of an architecture in encrypted code to be able to exchange non-public information material, such as for example the growth rate of new subscribers to the platform or even the exact number of such volume, has rendered itself completely ineffective in the face of scrupulous investigations by the SEC, which through its analysts and programmers has managed to objectively demonstrate that, on the basis of the conduct described in SEC v. Netflix insiders, the accused Mr. Sung, Mr. Joon, Mr. Junwoo, Mr. Lee and Mr. Bae, in connection with the purchase or

sale of securities (directly or indirectly) by the use of instrumentalities of interstate commerce or of the facilities of a national securities exchange[59]:

- *Employed device, schemes, or artifices to defraud*
- *Made untrue statements of material fact or omitted to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, and\or*
- *Engaged in acts, practices, or courses of business which operated or would operate as a fraud or deceit upon other persons, including purchasers and sellers of securities*

Each of them therefore acted in full violation of Section 10(b) of the Exchange Securities Act, in detail 15 U.S.C. § 78j(b):

To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any security-based swap agreement any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors

And in violation of Rule 10b-5, in detail 17 C.F.R. § 240.10b-5-1: Trading on the basis of material non-public information in insider trading cases, discussed previously.

As noted in the "Prayer for relief" section of the SEC filing, Mr. Sung, Mr. Joon, Mr. Junwoo, Mr. Lee and Mr. Bae are ordered to pay a civil penalty under Section 21A of the Exchange Securities Act, in detail 15 U.S.C. § 78u-1 – Civil penalties for insider trading and further, barring Mr. Sung under Section 21(d)(2) from acting as an officer or director of any issuer that has a class of securities registered under Section 12 or that is required to report files under Section 15(d).

Finally, the SEC obtained final judgments against Netflix's insiders through the Litigation Release No. 25438 / July 6, 2022[60] in which the United States District Court for the Western District of Washington judged all "insider ring". Mr. Sung, Mr. Joon, Mr. Chon and Mr. Lee consented to the entry of final judgments that resolved all claims and permanently enjoin each of them from violating the provision of Section 10(b), in addition Mr. Sung have agreed to an

[59] SEC v. Sung Mo Jun et al., First Claim for relief, Violations of Section 10(b) of the Exchange Act and Rule 10b-5 Thereunder (Against Defendants Sung Mo Jun, Joon Jun, Junwoo Chon, Ayden Lee, and Jae Hyeon Bae)

[60] Litigation Release No. 25438 / July 6, 2022 – available at https://www.sec.gov/litigation/litreleases/2022/lr25438.htm

officer-director bar. The Court also established a civil penalty of 72,875 dollars to Mr. Bae. Moreover, Mr. Sung was sentenced to 24 months in prison and was ordered to forfeit 495,000 dollars; Mr. Joon was sentenced to 13 months in prison and 1.11 million dollars to forfeit; Mr. Chon was sentenced to 14 months in prison and 1.58 million dollars to forfeit, finally Mr. Lee was sentenced to three years of probation.

Despite the final verdict against Netflix insiders, the issue of the sharing of sensitive data and confidential information with employees by listed companies such as Netflix is still a matter of public debate today, which in doing so are exposed to risky leaks of non-public information that could be harmful in the eyes of investors and the markets. Nonetheless, giving your employees access to corporate information that may be considered sensitive is part of the ethics and philosophy of Netflix, Inc.'s founder Reed Hastings who, as himself wrote in his 2020 book "No Rules Rules: Netflix and the Culture of Reinvention", making those details known is one of the best motivational tools for workers. This work ethic can be judged imprudent or risky from a legal-normative point of view but, results in hand, there is no doubt that Netflix has achieved impressive goals in the streaming sector and perhaps one of the main factors of this success lies precisely in dealing with their workers as members of a family who are told "how the day was" (the results and daily performance in the specific case of Netflix employees). Hastings himself was therefore aware that one day what everyone expected could happen, that is, that there was a leak of news or that some employees used such non-public data to profit from it illegally. In any case, after the scandal and the final conviction of the now former Netflix employees, nothing has changed as regards the disclosure and sharing of non-public information to its insiders by Netflix and its subsidiaries.

2.3. Elon Musk case

In the first part of this chapter, our analysis focused on a specifical topical case of insider trading through SEC v. Netflix insiders in which the common thread of all our reasoning was mainly the violation of an internal company policy and the illegal conduct regarding the disclosure of material non-public information and its exploitation in the practice of trading in Netflix securities. In this part however, we will analyse another specific case even more topical in reference to the allegations made by the SEC against Elon Musk, known founder of Tesla among others, with regard to the manipulation of the market through the abuse of

disclosure tools such as social networks (specifically Twitter) and through the public disclosure of fake news-material information.

We will therefore try to examine in detail the allegations against Elon Musk via "SEC v. Elon Musk"[61] providing food for thought on the use of social networks as weapons of market manipulation, the public dissemination of fake news by official social profiles to the public and the debate regarding freedom of expression or speech on the web vs legislation on market abuse and insider trading. Furthermore, as we did for Netflix, we will also try to analyse Tesla's corporate policy regarding the code of ethics, insider trading and the use of non-public information material to understand how its founder could have been sentenced.

In the Summary[62] of the aforementioned document, we immediately find the central theme of the entire executive procedure, i.e., a long series of sentences and public statements made by Elon Musk, Chief Executive Officer of Tesla, Inc., starting from August 7, 2018, concerning his publicly traded company and the will to make it private in the future. These statements were made public through the official profile of the Tesla founder on the Twitter social network, one of the most famous and used worldwide, together with Facebook and Instagram. Starting from early August 2018, his "tweets" have falsely suggested to his followers and to the whole world, given the importance of the profile and the large number of people who follow Tesla on Twitter and the trend of his performances, that he was virtually certain that he would bring Tesla into a private company regime on the basis of a purchase price that would include some sort of premium for those currently holding Tesla's shares, that the entire public-to-private transition would be assured procedurally and financially, and that this operation would depend on the results at the end of the day of his survey addressed to followers: Private YES or Private NO.

By declaring this kind of information, objectively considered as substantially relevant information regarding the direct effects it could have on the share price and on the reaction of investors, Mr. Musk failed to specify as many relevant data for a multi-billion dollars transaction such as for example key deal terms, price, or any potential funding source as collateral. The beginning of this social activity by Elon Musk began around 13.00 on August 7, 2018, with his tweet:

[61] SEC vs. Elon Musk, Case 1:18-cv-08865, Document 1, Filed 09/27/18

[62] Ibidem, Summary, page 1

"Am considering taking Tesla private at 420$. Funding secured"[63]

This tweet then turned out to be false and misleading as in the following three hours Mr. Musk added further ancillary statements accompanying the first tweet which also turned out to be completely false and unfounded such as:

"*My hope is current investors remain with Tesla even if we're private. Would create special purpose fund enabling anyone to stay with Tesla. Already do this with Fidelity's SpaceX investments."*[64]

"Investor support is confirmed. Only reason why this is not certain is that it's contingent on a shareholder vote."[65]

[63] Figure 1. Captured from Twitter account of Elon Musk
[64] Figure 2. Captured from Twitter account of Elon Musk

Moreover, these statements turned out to be not only false but also devoid of any foundation that could make Mr. Musk think he was disclosing such information to the public. Moreover, it was noted that at the material time he had never yet discussed or negotiated a possible transition of Tesla at a price of $420 per share with any potential funds or resources, just as he had never inquired about the real possibility that all Tesla investors could actually continue to hold the shares as a private company. Even Mr. Musk had never yet received any confirmation from Tesla or SpaceX regarding the provision of investor support as he praised on Twitter, much less did he know that he had not yet fulfilled his legal obligations regarding numerous additional contingencies for a going-private operation by instead leaking through his profile that any obstacle that separated Tesla from becoming a private company was his personal will and a simple majority vote by the shareholders.

As noted by the SEC, and as inevitably everyone might have expected in those exciting hours, investors immediately reacted promptly to Elon Musk's tweets, so much so that from the time of his first tweet that day until the close trading on August, 7, Tesla's stock price increased by more than 6% on significantly increased volume and closed up 10.98% from the previous day. From these simple but very clear data it can be seen without any doubt that the public declaration of Mr. Musk though his official profile on Twitter and above all his omissions of clarifications in this regard have significantly created confusion and destabilization in the market for Tesla's stock and reflex caused chaos among investors.

2.3.1. SEC vs. Elon Musk

[65] Figure 3. Captured from Twitter Account of Elon Musk

As in the Netflix insiders' case, also in this compliant case the SEC proceeds with the classification of the main accused, i.e. Elon Musk, 47 years old, co-founder and Chairman of Tesla, Inc. since 2003 and named Chief Executive Officer since 2008. From his leading roles within the company, therefore, Mr. Musk has the task of supervising and directing all product development, engineering and design of Tesla's product. Next, the classification of Tesla, Inc. after its initial public offering in 2010, whose common stock was registered with the Commission pursuant to Section 12(b)[66] of the Exchange and Securities Act of 1934 and publicly traded on Nasdaq Global Select Market under the symbol TSLA. As it is now known globally, the company's core business is the design, development, and production of electric vehicles and energy generation\storage systems to be sold at its stores and subsidiaries worldwide[67].

As happened in the case analysed at the beginning of the chapter, we then find the so-called "Factual Allegations" which exhaustively contain the actions and behaviours that the SEC examined to formulate the accusation against Elon Musk regarding the use of Twitter to disclose "fake-material information" in an unlawful manner according to the legislation on insider trading and market abuse. Below a brief summary list of these factual allegations[68]:

- Mr. Musk used the social network Twitter to communicate with millions of people as the spokesperson of Tesla,
- Mr. Musk's tweets regarding Tesla "short-sellers",
- Preliminary discussion regarding taking Tesla private,
- Going-private transaction between Mr. Musk and Tesla's board of directors,
- The Seven August's tweets and the market's reaction,
- Additional Mr. Musk's tweets on August, 13,
- Materially false and misleading statements of Mr. Musk,
- Mr. Musk omitted material facts and the duty not to knowing his tweets were false,
- Chaos reaction in the market and harmed Tesla investors.

[66] 15 U.S.C. § 78l(b)
[67] SEC vs. Elon Musk, Defendant – Relevant Entity
[68] Ibidem, personal formulation of Factual Allegations

Analysing in detail the main parts of these arguments expressed by the SEC in the official accusation against Mr. Musk, it is useful to dwell first of all on the public figure of Elon Musk and his presence in the world of the internet and social networks. Starting from 2009, he immediately began to undertake a social communication process only through Twitter via his official profile https://twitter.com/elonmusk , so much so that in all other social networks and the most used platforms in the world such as Facebook or Instagram we only find the presence of fake pages or fun clubs of the multi-millionaire. Mr. Musk immediately began to communicate information and news regarding Tesla's business on Twitter, so much so that the Chief Financial Officer had defined his profile, which was increasingly followed and became viral over the years like the profile of today's "influencers", as a strong marketing channel for Tesla and its subsidiaries given that by now it was a real constantly updated information forum on the development of Tesla and its products coming from an authoritative source as that of its co-founder. It is therefore easy to understand how over the years the figure of Elon Musk has increasingly become a point of reference and a spokesperson for his company, so much so that his profile currently has more than company, so much so that his profile currently has more than 26 million "followers". From a legal point of view, on November 5, 2013[69], Tesla officially formalized through a public document to the Commission that Mr. Musk's Twitter account would be used from then on as the main information channel regarding the public disclosure of announcing material information to investors about Tesla's products and services, even encouraging the public to follow this profile to stay up to date on publications concerning the company. Since that day, thousands and thousands of tweets have been published by Mr. Musk and these statements have therefore become instantly available to anyone with access to the Internet via any available device; it can be said that Tesla was one of the first companies in the world to have used a social network as the main point of reference for investors and for public disclosure of material information.

Another important topic to take into consideration in this analysis is the theme of the so-called "short-sellers" towards Tesla. In 2018, investors and financial analysts began to wonder with growing concern whether the company would be able to meet its production goals based on previous statements, given that at that time Tesla needed to start earning sufficient cash in order to sustain its operations and pay its existing debt load. In august 2018, more than 13

[69] Ibidem, at Factual Allegations – Musk Used Twitter to Communicate with Millions of People as Tesla's Spokesperson

billion dollars of Tesla shares were officially shorted[70] causing a quite furious reaction from Elon Musk who declared via tweet that he would do everything to be able to eliminate shorting activities once and for all with respect to Tesla securities which, according to him, has always been the victim of short sellers over the years (in some tweets he even went so far as to write that they would be burned[71] and that they would have a maximum of three weeks of life before the explosion of their market positions in June 2018).

In proceeding therefore with the analysis of the factual allegations, we arrive at the central point of the entire procedure, namely Mr. Musk's idea of undertaking a transition to make Tesla a private company. The first step is made to coincide by the SEC with some meetings in January 2017 held between Elon Musk and the representatives of a foreign investment fund in which, according to Mr. Musk, the fund verbally expressed its desire to plan a huge investment in Tesla with the related transfer of the entire production chain to the Middle East. After a long pause for reflection between the two parties, in July 2018 the representatives of the fund decided to request a further planning interview with Elon Musk which was then also attended by the chief of Tesla staff and Tesla's CFO. During this approximately 45-minute interview, according to the reconstructions of Mr. Musk's explanation of the facts, he learned that the fund had already purchased approximately 5% of Tesla's common stock on the open market as further concrete confirmation of the fact that it was seriously considering taking Tesla private. However, during this meeting, Musk explained to the SEC that although there were no further agreements or preliminary statements regarding the terms of the agreement, he learned that the principal representative of the fund would like to enter into a standard going-private transaction. Furthermore, it was again proposed to start establishing a production facility in the Middle East even if Mr. Musk thought that this was not an essential precondition for the success of the entire operation to him this depended only on the amount of capital the fund was required to commit. The strangest thing is that, from what was reconstructed by the SEC, this conversation never even mentioned some fundamental issues for a going-private transaction process of that scope and importance such as:

- Money amount or specific ownership percentage for fund's investment,

[70] "To short" means shares sold by investors who do not own them at the time of selling which believe the price of the stock will fall and hope to buy it at lower price to cover their "short" positions earning profits. On the contrary, if the stock's price rises, short sellers who then exit their positions by purchasing the stock at higher price, will incur in losses.

[71] Elon Musk's tweet: "Oh and uh short burn of the century coming soon. Flamethrowers should arrive just in time", May, 4, 2018 - https://twitter.com/elonmusk/status/992388944774938626

- Acquisition premium to be offered to current TSLA shareholders,
- Possible restrictions on foreign ownership of a significant stake in Tesla,
- Available liquid capital of the fund,
- Historically experience of the fund regarding others going-private transactions,
- The necessary Tesla's board approval of the entire operation[72]

In addition to these incomplete omissions of details, it was discovered that the fund would have been in favour of proceeding with a "reasonable" going-private transaction and that Elon Musk was requested to establish his requirements to complete the transaction. Again, however, nothing was established in writing and no document or confidentiality agreement was agreed or discussed. Mr. Musk then had no further contact with fund representatives until August 10, 2018, which was three days after he tweeted about the idea of taking Tesla private.

Subsequently, the SEC points out that only on August 2, 2018, Mr. Musk decided for the first time to send an official request to Tesla's Board of Directors and General Counsel via an email with the subject line "Offer to take Tesla private at $420". In the text of this email, among other arguments, we still find Elon Musk's firm will to be able to eliminate the negative effect that according to him the short-sellers had had up then on the company's share performance. Furthermore, he declared that this proposal should have been submitted to the shareholder's vote as soon as possible and that he himself had calculated a 20% "standard premium" with respect to the value of Tesla's market shares. In addition to the fact that this calculation was made on the basis of an individual subjective estimate by Elon Musk, the price of $420 per share was not even exact: starting from the current market valuation, it would have reached a total of $419 per share but, according to Mr. Musk, a price of $420 would have been more attractive from the point of view of marketing and psychological perception (as further proof of how subjective this estimate was and absolutely devoid of financial foundation, Elon Musk argued in the email that, according to his girlfriend, that number was quiet "funny" as a price compared to 419 and who had recently begun studying the psychological meaning of numbers through marijuana culture). The SEC then found further evidence confirming the fact that Elon Musk had never before even hinted at such a price with no potential fund to take Tesla private and that, according to his statements, he was 50-50 sure at the time that this transition would take place without any problems and at the price set by him. The response from the Tesla board was very quick: after learning from Mr. Musk that a potential fund was about to make the operation possible, the board pointed out

[72] Ibidem, at Preliminary Discussions Regarding Taking Tesla Private

that from their point of view it would have been very difficult for the small investors to be able to remain holders of Tesla's shares even if he strongly wanted all current investors to remain so even after the transition. To try to satisfy his request, the board therefore decided to authorize Elon Musk to contact certain types of current investors to understand their effective interest in such a proposal[73].

As further evidence of Elon Musk's illegal conduct, the SEC proceeds to enumerate a series of facts or events that should have somehow occurred between the day of the last meeting with the fund and the day of Mr. Musk's public statement on Twitter of his desire to make Tesla private which can be summarized in some fundamental shortcomings:

- Total lack of further calls or meetings or contacts of any kind between Elon Musk and the representatives of the fund,
- No specific reference to a going-private transaction of $420 per share with any prospective fund,
- No confirmation or further contact, after having had a conversation regarding a privatization process that took place with an equity fund, with further potential strategic investors to ensure effective interest in this transaction,
- No reports, files, documents regarding specific proposals or written agreements regarding this process to Tesla's Board,
- No contact or communication to current shareholders to ask for feedback on their interest in remaining with Tesla even if it went private,
- No request to external or internal advisors for assistance regarding the procedure of a going-private transaction,
- No request for confirmation to understand if retail investors could have continued to invest in Tesla in the case of private,
- No information on possible restrictions on illiquid holdings for institutional investors,
- No prior determination of what regulatory policy would have required this type of transaction and whether there were any mandatory requirements to be met before proceeding with the transition.

Despite this, on August 7, 2018, Elon Musk published the aforementioned tweets on his official Twitter profile regarding the desire to make Tesla private. As reported by the SEC,

[73] Ibidem, Musk's Discussion of a Going-Private Transaction with Tesla's Board of Directors

about 35 minutes after the fateful tweet, Tesla's Chief Financial Officer decided to ask for clarification on this and if he had an official communication to make known to the board, employees and potential investors, via direct message on his telephone, adding that if he had wanted he would have taken steps to write an email to the entire Tesla structure in his own hand and to an official statement on a public Tesla blog. Mr. Musk's response was affirmative even though, as listed above, it can be clearly assumed that at the moment he essentially had nothing concrete to be able to tell the whole world that Tesla would go private for a 420$ share.

As mentioned at the beginning, Tesla, Inc. is a company listed on the Nasdaq, in which there are additional rules and directives to be compulsory followed, including the one regarding the disclosure of material information: every company listed on the Nasdaq must notify at least up to ten minutes before the publicly release of material information regarding corporate events like a proposal of a going-private action. However, having not informed himself about this, among other things, he did not even fulfil this obligation and therefore Nasdaq, following Mr. Musk's tweet, halted trading in TSLA shares (which in meantime had skyrocketed in market negotiations due to this unforeseen unexpected publication).

Only after about two hours, Mr. Musk sent the first email communicating to Tesla employees with the subject "Taking Tesla Private" which was also published in the company's official public blog. Therefore, for the first time, two hours after his announcement to the whole world, Tesla's shareholders were warned of the imminent transition to a private company through a final vote, according to Mr. Musk's email, and that they would have to choose whether to keep the own positions or sell them out at $420 per share. A few minutes after this email, Elon Musk tweeted again that investors support for the transition was confirmed and that the only thing left to be defined was the shareholders' vote for final approval, a statement which, as noted above, turned out to be avoid of any foundation. Following the permitted resumption of TSLA trading on the Nasdaq, the stock price continued to grow, reaching +6% just a few hours after the first "going-private tweet"[74].

As further proof that the entire Tesla Board of Directors was absolutely unaware of the entire privatization process so acclaimed by its Chief Executive Officer, the SEC provided a long series of requests for clarifications which reached Tesla's head of Investors Relations immediately after the publication of the various tweets by Elon Musk by numerous investors, stock analysts and journalists, and the ambiguous unclear responses by Tesla. Even some

[74] Ibidem, Musk's August 7 Statements and the Market Reaction

investment banks and friends of Mr. Musk began to ask if he was joking or, if not, if there were other information regarding the operation as previously mentioned. The only responses from the head of Investors Relations to the increasingly incredulous and furious requests were simply that the only information he could provide were those listed on Elon Musk's official Twitter profile and via Tesla's public blog[75]. It can be said that in those hours all the major newspapers, investments banks and Tesla investors were completely shocked by those announcements as much as Tesla itself which in fact began to ask Mr. Musk more and more assiduously to provide further documentation or agreements undertaken for initiating such an operation.

Subsequently, for another six days, Mr. Musk continued his process of publishing content regarding the going-private Tesla's transition, including various tweets towards the short-sellers who, according to him, would soon be just a memory. After a news blog published a post on the internet on August 12, 2018, stating that some sources inside the previously mentioned fund had revealed that where was indeed an interest in this transition but that nothing had been discussed until then to the company's decisions, whether to proceed with its increase in stake and more.

The following day, for the first time, Elon Musk published a post entitled "Update on Taking Tesla Private" on the official Tesla blog in which he finally found some more information about his previous tweets: he explained that his tweet of August, 7 was based on his personal impression and feeling that an agreement with the fund would soon be found and that, for the first time, he was currently in contact with the fund and other investors to discuss the whole process of privatization but that no detailed proposal had yet been presented. Other than the fact that this post said the complete opposite of his August 7 tweet, Mr. Musk did not give any other information regarding the "$420 per share" and the fact that this price had not yet been agreed upon or negotiated.

Finally on August, 24, 2018, a blog post was cleaned up on Tesla's public blog announcing that Elon Musk had abandoned the process of attempting to take Tesla private, also for the first time, he then disclosed the obstacles to allowing current Tesla investors to remain invested if Tesla went private and thus corrected his multiple previous misstatements that any going-private transaction would allow all current shareholders to remain invested (next trading day Tesla stock closed down over 15% from the closing price of the August, 7' one)[76].

[75] Ibidem, Reaction to Musk's August 7 Statements
[76] Ibidem, Additional Statements by Musk on August 13

Continuing the analysis of SEC vs. Elon Musk, we therefore arrive at the definition of a whole series of actions and publications that were subsequently deemed false and misleading with regard to the legislation on public disclosure of material information. Indeed, Mr. Musk made multiple materially false statements whose left market participant with the false and misleading impression that if he would choose to take Tesla private at $420, the only outstanding requirement to be satisfied was a shareholder vote[77]:

- The subsequent tweets regarding "funding secured" and "investor support confirmed" are misleading as he actually had no certainty nor any agreement that could confirm any amount of funding,
- The statement regarding the "shareholder vote" was false and misleading as any going-private transaction would have required approval of Tesla's board or a specially-appointed committee of the board and up to that moment no formal proposal had ever been presented
- No deal terms had been agreed upon any source of funding and any large investment to fund such transaction would have been predicated on terms the parties would have to negotiate (for example, the building of a production facility in the Middle East requested by the fund),
- He created misleading impression that certain terms of the transaction had been determined when, in fact, they had not even been explored or proved to be impossible.

Finally, as seen for Netflix insiders, we find the official condemnations by the SEC for the final sentence against Elon Musk. He was first requested to formulate the final conviction on the basis of your unlawful conduct in violation of Section 10(b) of the Exchange Act and Rule 10b-5, and to order to disgorge any ill-gotten gains received as a result of the violations cited in precedence. In addition, he was required to impose a civil fine in monetary terms under Section 21(d)(3) and to prohibit future roles as an officer or director of any issuer that has a class of securities registered under Section 12 or that is required to files reports under Section 15(d).[78]

[77] Ibidem, Musk's August 7 Statements Were Materially False and Misleading, Musk Knew or Was Reckless in Not Knowing that His Statements Were False and Misleading
[78] Ibidem, Prayer For Relief

2.3.2. Tesla Code of Business Ethics

In a similar way to the case of Netflix Insiders, also in this part of the chapter we will try to analyse the code of conduct and the corporate policy of Tesla regarding insider trading and treatment of material non-public information. On the official Tesla website, in the "Corporate" section, we find all the public documents concerning the company and internal policies, including the "Code of Business Ethics". Within this document we also find the part concerning the topic of insider trading and the actual documentation available to all members of the Tesla structure.

It is interesting to note in this case how Tesla's code of ethics immediately introduces the fact that this document is addressed to and applies to all directors, officers and employees and that anyone who violates this Code may be subject to discipline, even termination. The document tries to establish basic principles to be followed in an attempt to avoid possible charges or convictions for unlawful behaviour by workers and to safeguard the business ethic pursued over the years by Tesla, i.e. make the world a better place through its products and services in a working environment permeated by ethical principles of respect and continuous improvement to make the company increasingly capable of achieving its goals and overcoming the challenges of the future[79].

Unlike Netflix's insider trading policy, in Tesla we find first of all a real code of conduct for the company that is expected to be respected and followed by all its employees and directors, and then follow the specific directive on insider trading. It is interesting to note how the entire code of ethics addresses the person who is reading it in the first person and asks questions for reflection in the event that an individual finds himself in an ambiguous situation in which he does not know how to proceed or act on the basis of his role within the company, such as whether the type of behaviour to engage in that specific situation is legal or not, whether it is consistent and does not violate Tesla's code of ethics and expectations, or whether this action is in the best interest for the company.

As for insider trading part, the document establishes that, quite similar to Netflix's philosophy, Tesla insiders could come into possession of material non-public information about upcoming product announcements, financial results or the number of vehicles produced and sold, innovations and others. This inside information could therefore have a significant effect on Tesla's stock price; therefore, it is expressly requested that insiders could only trade Tesla stock when relying upon publicly available information. Moreover, the document also

[79] Tesla Code of Business Ethics

treats the practice of tipping, i.e. any act of disclosure of such information to persons external to Tesla, including family members, household members and friends, is expressly prohibited, as tipping others is as illegal as engaging in insider trading themselves.

It is also established that the same rules also apply in the event that insiders become aware of material non-public information of other Tesla partner companies or its subsidiaries (exactly as in the Netflix policy). Finally, it is reiterated that this code of conduct must be complied with by following in detail the corporate regulation relating to insider trading, available from Tesla's Legal Department, the office in charge of assisting and coordinating the supervision of the trading operations, exactly as the Compliance Officer at Netflix, Inc.

In addition to the purely promulgated policy for insider trading aimed at all Tesla employees, which expresses rules to be followed very similar to what was observed in Netflix case (Open Trading Windows, special black-out periods, legal filing to disclose, …), it is interesting to note that on the last page there is a further code of ethics addressed directly to Tesla CEO and Senior Financial Officers. It is interesting to analyse this section in detail precisely because, as we will see, every directive of this code was violated or not followed by Elon Musk, co-founder and Chief Executive Officer of Tesla at the time. The CEO and senior officers are subject to the following additional specific rules[80]:

- They are responsible for full, fair, accurate, timely and understandable disclosure in the periodic reports required to be filed by Tesla with the SEC. They have the responsibility to promptly bring the attention of the Disclosure Committee any material information of which insider may become aware that affects disclosures made by Tesla in its public filings or otherwise assist the Committee in fulfilling its responsibilities as specified in Tesla's Disclosure Controls and Procedures Policy
- They have the responsibility to report to the Disclosure Committee and the Audit Committee any information concerning significant deficiencies in design operation of internal controls which could affects Tesla's ability to record, process, summarize and report financial data; any fraud, whether or not material, that involves management or employees who have significant role in Tesla's structure
- They have the responsibility to report to General Counsel or Legal Department any information concerning possible violation of the Code of Business Ethics, including conflict of interests

[80] Ibidem, Code of Ethics for CEO and Senior Financial Officers

- They have the responsibility to report to General Counsel any information that could be evidence of a material violation of the securities or other laws, rules or regulations applicable to Tesla and its business
- The Board of Directors shall determine or designate appropriate persons to determine actions to be taken in the event of violations of the Code of Business Ethics or of these additional procedures by the CEO and Tesla's senior officers. These written notices shall include demotion or re-assignment of the individual involved, suspension with or without pay or benefits, and the termination of the employment.

2.3.3. Conclusions

On October 16, 2018, the final judgment was officially published against Elon Musk regarding his unlawful behaviour in the field of material information and market abuse. In the final act[81] we therefore find, in addition to the sentence, a settlement agreement signed between Elon Musk and the SEC which is interesting to analyse. In this agreement, signed by both Mr. Musk and the official appointed by the SEC and by a public notary, it is established that the convict is permanently restrained and joined from violations of Section 10(b) of the Securities and Exchange Act of 1934 and Rule 10b-5, and that a monetary penalty totalling $20 million be ordered.

Furthermore, it is also agreed that Elon Musk must retire from his role as Chairman of the Board of Directors of Tesla, Inc. for a period of at least three years, which could be extended at the discretion of the Commission at the end of the three years. It is also established that he must comply with the new directives implemented by Tesla regarding everything that has to do with public disclosure of information about the company and its business such as the disclosure of posts on social media (for example posts on Twitter, official statements via the company website, press conferences or calls\conversations with investors). Moreover, it is required that before carrying out any of the aforementioned actions, a pre-approval of his statements is certified with a specific written document containing material information from the Tesla Board of Directors.

Additionally, each of these written pre-approvals must then also be submitted in narrative form and supported by evidence that they have actually pre-approved by the Tesla Board, to the designated SEC for this specific case and to the office of Chief Counsel of the

[81] SEC Vs. Elon Musk, Final Judgment, Case 1:18 – cv – 008865 – AJN – GWG, document 14 filed 10/16/2018

Enforcement Division not later than at least 14-days prior to the date of the event (conference, web publication, social media post, …).

From this final sentence it clearly emerges how the SEC has tried in every way to be able to control in some way any future declaration by Elon Musk regarding material information that could have had disastrous effects (as in fact happened in August of 2018) in the markets, with the primary purpose of safeguarding and protecting investors and secondly of safeguarding Tesla company itself against unlawful behaviours by its officers and directors. As in the case of Netflix, here we find too a pecuniary compensation (much more substantial, as much as 20 million dollars) for the illegal conduct adopted by Mr. Musk though his public statements on his official Twitter profile. However, we do not find a total ban against him regarding the private management of his social accounts but rather a sort of Orwellian "Big Brother" for everything concerning his future statements about Tesla or its partner companies. It could even be said that in addition to total supervision, a sort of "media cage" has been applied within which every single statement by Elon Musk cannot be disclosed or published without prior approval by Tesla and the SEC.

The much exuberant and perhaps abusive behaviour of Mr. Musk on social media has therefore led to the inevitable conclusion that, in order to avoid again that events similar to those analysed in the previous paragraph can happen again given the large volume and frequency of tweets that he makes public to millions people, a supervisory approach has been displayed on all possible channels that he has, and will have, available such as press conferences, Tesla public blog posts, tweets, calls or conversations with Tesla investors or partners.

However, it is also useful to note, although Elon Musk has in practice violated every single point of the ethical code of conduct established by Tesla for its employees, officers and directors, a warning has not been officially published by the company or the Tesla Board of Directors. So much so that, currently, in the "Corporate Governance" section of Tesla's official website, we will find the figure of Elon Musk within both the corporate leadership and a member of the Board of Directors. It therefore seems that the much ostentatious code of ethics and corporate conduct (with even further specific rules for Tesla's officers and directors) has actually been put on standby towards its co-founder. In any case, the final decision of the SEC, respecting what Tesla established, did not promulgate further obligations regarding the prohibition of the further use of Elon Musk's profile as a primary information channel for investors regarding Tesla material information, thus respecting the decision taken by the company itself in 2013.

It therefore arises spontaneously to ask whether it is actually possible for a world-renowned multinational like Tesla, Inc. to detach itself, even after a final sentence of this magnitude, from one of its main figures or even a vital figure for the continuation of the company's business expansion or to strengthen the company's image around the world. The same code of ethics, supervised by Elon Musk himself, has therefore been the subject of complaint as much as lack of complaint against those who should, due to their corporate role and public image and influence, be the first to "set a good example" of conduct to their employees and their colleagues, given that even many ideas of Tesla' ethics come from its co-founder.

Another complex aspect could arise from another point of view: detaching or definitively punishing a founding partner or to-much-important director for the entire company could in turn be seen as irreparable damage and as an irreversible action which could even cause greater damages (of corporate image and stability) with respect to the vision of instead not acting against him so as not to further exacerbate the sentence already promulgated by the Commission even if all the rules of ethical conduct have been violated.

3. Chapter 3 – New provisions and final conclusions

3.1. Introduction

In the first chapter we have tried to analyse and summarize the laws on insider trading and market abuse mainly in the United States and Europe, the two oldest and most important stock markets in the world, with a mention also of the legislation in an increasingly emerging market and dominant like the Chinese one.

In this last chapter we will try to analyse the current proposals for the future with reference to some changes, which seem to be increasingly requested by investors and political authorities, in an insider trading regime to modernize the legislation in force in Europe, China and the United States. We will therefore begin with an explanation of the new changes that will officially take effect from February 27, 2023, in US with reference to Rule 10b-5 and Section 10 of the Securities and Exchange Act 1934 and the new proposals promoted by the Chairman of the Securities and Exchange Commission in relation to corporate insiders and the issue of market abuse by members of the Congress.

We will proceed in succession with the analysis of the latest changes to the European Directives on insider trading and the explanation of the current regime in the various states and we will consequently explain the main differences and similarities between the new EU and US laws. Finally, we will try to focus on the Chinese legislature, with particular interest in the new policies with reference to market abuse.

Subsequently we will try to draw conclusions and purposes for thought from what emerged from the observations of Chapter 2 on the specific cases of insider trading and market abuse (Netflix, Elon Musk) also focusing on the issue of the use of social media as a weapon for disseminating material information and how this can have a real and concrete reaction in the financial markets.

3.2. Regulatory changes in US

"Congress enacted the Federal securities laws to promote fair and transparent securities markets, avoid frauds, and substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the securities industry. The securities laws' antifraud prohibition that proscribes certain insider trading, including Section 10(b) of the Exchange Act, play an essential role in maintaining the fairness and integrity of our securities markets. The Securities and Exchange Commission has long recognized that insider trading and the fraudulent misuse of material nonpublic information by corporate insiders' harms not only individual investors but also undermines the foundations of our markets by eroding investor confidence. Congress has recognized the harmful impact of insider trading on multiple occasions, such as by providing for enhanced civil penalties specifically for insider trading".[82]

On December 14, 2022, the Securities and Exchange Commission was called to vote to definitively decide what were the new regulations[83] to be adopted in addition and\or modification on the affirmative defense to insider trading liability and new disclosures related to insider trading and market abuse.

In particular, we find a new rule concerning the new conditions to the affirmative defense to insider trading pursuant to a contract or plan to satisfy the requirements of the Securities Exchange Act 1934, Rule 10b5-1 (c)[84].

Furthermore, we also find the introduction of a new periodic disclosure requirements related to insider trading, with respect to company insider trading policies and procedures for adopting Rule 10b5-1 plans by directors, officers, employees. Related to this, it is specified that officers' equity compensation awards must close in time to the company's disclosure of material non-public information.

Finally, the identification of transactions made pursuant to regulations' report plan on Forms 4 and 5 is introduced (plans also referred to, for example, within the insider trading policies of Tesla and Netflix), and the declaration of "bona fide" gift to be reported within two business day rather than after year-end of standard forms. Companies will therefore be officially

[82] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86 – Introduction, page 5

[83] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86

[84] 17 CFR 240.10b5-1 – Trading "on the basis of" material nonpublic information in insider trading cases.

required to update and adapt to the new regulations through their delegated offices in the first filing that covers the first full fiscal period that begins after February 27, 2023.

In addition to the companies, which will therefore have to comply with the new legislative changes regarding periodic disclosure requirements, corporate insiders (under Section 16 defined) will also be required to comply with the new requirements and obligations concerning Form-4 trading plans.

3.2.1. Cooling-Off Period conditions

Unlike what seemed to emerge from the first amendment proposals announced by the SEC, in the final provisions there is no reference to a possible “cooling-off” period for companies. On the other hand, however, it is established that corporate officers and directors must provide that trading under plans cannot begin until the later of:

- 90 days after the adoption of Rule 10b5-1 plan
- 2 business days following the disclosure of the company’s financial results or fiscal quarter in which the plan was adopted

Therefore, in a nutshell, the required cooling-off period for corporate officers and directors is capped at a maximum of 120 days after the Rule plan’s adoption, while for other employees the cooling-off period remains 30 days after-plan. In addition, we find other changes concerning the cooling-off period such as for example the new regulation that codify that any change to the amount, price, timing of purchase\sale (including change in written formula, algorithm) constitutes a termination of the plan and the adoption of a new plan, triggering the same cooling-off period.

The new amendments to this legislation make the regulation under the cooling-off period more complicated at a bureaucratic level as a substantial uncertainty is introduced as to when the first purchase\sale under the plan can occur is actually established. Indeed, the new rules contemplated 90- or 120-day period for corporate officers and directors, depending on what type of report Form is filed during the period (10-K for fiscal quarter results or 10-Q for other financial results).

We can conclude that the creation of the cooling-off period is intended to deter opportunistic trading that may be occurring under the “old Rule” and, as a consequence, it may increase investor confidence that corporate officers\directors are not using Rule 10b5-1 plans for the

purposes to publicly disclosure they future trading plans. The main scope of this provision is to provide a certain separation in time between the adoption of the plan and the commencement of trading under it with the scope of maximining the ability of an insider to benefit from any material non-public information.

"In addition, academic studies documenting abnormal trading results indicate that opportunistic trading may be occurring notwithstanding current Rule 10b5-1 (c) and that certain corporate insiders are earnings profits unavailable to others"[85].

One of the most frequent examples is that corporate insiders commonly have access to preliminary quarterly financial data before it is publicly released, and such data are the most important and frequent material information disclosure by the companies. The cooling-off period tries to avoid situations where an insider adopts a plan while aware of likely directional trends in quarterly results (or information related to other types of events like potential merger, acquisition, departure\new entry of a named executive officer) and trades before the disclosure of such material

3.2.2. Director and Officers certification

With reference to the adoption of Rule 10b5-1 trading plans by corporate officers and directors, the new changes regarding insider trading specify that they must include a disclosure certifying, at the time of the adoption of a new plan:

- They are not aware or in possession of material non-public information about the company or its securities
- They are complying with the plan in good faith and not as a part of a scheme to evade the prohibitions of the Rule

Typically, as seen in Netflix and Tesla corporate policies concerning insider trading and market abuse, these trading plan form documents are specially prepared or compiled by broker-dealers or otherwise specifically experienced individuals within the companies' compliance offices. Consequently, it should always be noted that the counsel for directors and officers should always be responsible for reviewing the plan to ensure that this new

[85] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86 – page 28

representation is included in any new or modified Rule 10b5-1 plan entered into after February 27, 2023.

This new kind of "certification" condition is intended to reinforce directors' and officer's cognizance of their obligation not to trade or enter into a trading plan while aware of material non-public information about the issuer or its securities.

"It is their (corporate insiders) *responsibility to determine whether they are aware of material non-public information when adopting Rule 10b5-1 plans, and that the affirmative defense under Rule 10b5-1 requires them to act in good faith and not to adopt such plans as part of a plan or scheme to evade insider trading laws"*[86].

As we have seen in Netflix case or Tesla case, especially regarding the numbers of new subscribers available to Netflix employees, corporate insiders are often aware of material non-public information and subject to their confidentiality obligations, they can consult with experts to determine whether they can make their representation truthfully or the addicted legal company's counsel can assist insiders in understanding the meaning of "material non-public information" (remember Netflix Insider Trading Policies and Tesla's Code of Business Ethics when we found sections related to their Compliant Officers to help and assist insiders in their trading plan filing).

In addition, to the extent that directors and officers provide issuers with these new compliances, they would likely have a possible greater effect on investor confidence and trust that the officer\director in fact was not aware of material non-public information when making the representation due to the issuer's close relationship to its officers and directors.

3.2.3. Overlapping plans

With reference to this particular rule regarding prohibition on overlapping plans, an individual may not have another outstanding Rule plan for purchase\sales of any class of securities of the company during the same period. Based on this general rule, however, the new amendments propose different types of exceptions:

[86] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86 – page 42

- An individual is lawfully allowed to have two or more separate Rule10b5-1 plans as the later-commencing plan does not begin trading during the cooling-off period that would have applied if the later-commencing was adopted on the date the earlier-commencing terminates
- If all the trading plans presented meet all other conditions applicable to the report document files

In addition, it is also interesting to note a furthermore complex exception in reference to separate trading plans for "sell-to-cover" transactions in which corporate insiders order their agents to sell securities or financial products only to maximize or satisfy tax withholding obligations at the time an equity award vest. In detail, an insider is legally authorized to have one or more different plans so long as the additional plans only guarantee that sell-to-cover operations are carried out, in which only an agent authorized by the individual can automatically sell securities with the purpose mentioned above in connection with a compensatory premium and the insider has in no way personal control of the timing of the execution of these operations (which in fact take place semi-automatically after the pre-approval established by the insider to his agent in charge of executing such market transactions).

Moreover, we find the exception of the exceptions, i.e., the Securities and Exchange Commission does not deem it appropriate to allow this type of possibility in the event of exercise of option awards, as being able to exercise this right by insiders could create situations of risk of opportunistic trading.

Finally, it is also interesting to underline the fact that the final rules prohibit overlapping plans for any class of company's securities because, given the likelihood that the values of different classes of a given underlying (company securities) are highly correlated, allowing the use of multiple plans for trading in the securities of a company would allow for opportunistic behaviour risks.

3.2.4. Single-Trade plans restrictions

Another important new change made by the SEC with reference to Rule 10b5-1 concerns the restrictions on so-called single-trade plans. In general, the rule is that any individual is legally

entitled to have no more than one single-trade plan during any 12-month period. The modification relating to this concerns the possibility of a defense which will only be available for a single-trade plan that qualified for the affirmative defense (an ineligible plan does not preclude the possibility of the affirmative defense for another plan). Just as for the changes promulgated in the overlapping plans section, here too we find the introduction of an exception to this general rule for sell-to-cover plans. In this case, a sell-to-cover single trade plan is in fact specifically designated by the insider through an agent for the purchase\sale of securities in a single unique transaction. It is established that such a plan is not designed to affect a single transaction where:

- It leaves the agent discretion over whether to execute the plan as a single transaction
- It provides that the agent's futures actions will depend on events\phenomena not known at the time the plan is entered into

3.2.5. Quarterly Disclosure of Trading Arrangements

Under Rule 10b5-1 (c), the official mandatory documents to be disclosed by companies are Form 10-Q and Form 10-K regarding the last fiscal quarter. In order to satisfy the affirmative defense requirements, these specific files must contain within them any information relating to any director or officer adopted or terminated any contract or written plan for the purchase\sale of securities of the company or a "non-Rule 10b5-1" trading arrangement.

The latter type of plan is nothing more than a written trading arrangement that complies with the "old Rule" prior to these 2022's amendments but which does not comply with the new affirmative defense conditions. For greater clarity and transparency, the SEC has deemed it appropriate to declare under regulation that companies will also be required to indicate whether the plan is a Rule10b5-1 or a "old-Rule" plan and moreover to provide description regarding:

- Name and title of the corporate insider (director\officer)
- Date of adoption\termination of the plan
- Duration of the plan
- Aggregate number of securities to be sold\purchase

"... we view this information as necessary to better allow investors, the Commission, and other market participants to observe how directors and officers use Rule 10b5-1 plans and

other non-Rule 10b5-1 trading arrangements. The information also will add important context to other disclosures of trades by directors and officers, ... , and may aid investors in obtaining a more accurate valuation of the issuer's shares and making more informed investment decisions"[87].

Moreover, it will provide investors with valuable material information about specific uses of such arrangements which could bring focus to the particular arrangements and deter potential abuses.

3.2.6. Annual Disclosure of Insider Trading Policies

As analysed in Chapter 2, Tesla and Netflix have always adopted very similar insider trading and material non-public information policies over the years since both policies are largely inevitable extensions or reformulations of the cardinal principles issued by federal law which proposes a guideline to follow or to be taken as a model in order to be able to comply with the laws, especially on the subject of files reporting disclosure, tipping practice, corporate insiders behaviour.

With reference to the issue of public disclosure, companies will be required to disclose in Form 10-K or 20-F whether they have adopted or not insider trading policies or procedures governing the purchase\sale of their securities by corporate insiders or if the company itself have designated an "ad-hoc" compliance with insider trading legislation and any applicable listing standards. In the event that a specific insider trading policy has not been drafted, the SEC requires that there be a public document explaining the reason for this choice and that in any case there is a public copy of all procedures relating to insider trading and use of non-public disclosure materials to be submitted to the SEC through Form 10-K and Form 20-F files.

As a consequence, the SEC permits listed companies to post their policies and procedures on their website in lieu of providing disclosure in the filing, which allows a registrant to post its code of ethics on its website and disclose the internet address in its annual report to satisfy the code of ethics disclosure requirement (like Tesla and Netflix, Chapter 2).

[87] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86 – page 77

"Information about efforts an issuer undertakes to prevent misuse of its material non-public information is likely to be important to investors ... (because) ... *it provides greater transparency and assurances of the reliability of its disclosures to investors"*[88].

3.2.7. Disclosure of Equity Awards – Release of Material Non-Public Information

We find a further novelty regarding companies' executive compensations, i.e., they have to discuss their insider policies about the timing awards of stock option or stock's right in relation to the public disclosure of material non-public information concerning the company itself. In doing so, it is also necessary to predetermine how the board has established when to grant such premium through specific pre-approved documents or schedules. In addition, the SEC also requires that it must be determined, if this option is considered, whether the board\committee considers material non-public information in determining the timing of such terms and whether the company has also timed the public disclosure of such material for the purpose of affecting the total value of executive compensations.

In order to achieve maximum transparency and precision, the SEC also adds that if, during the last fiscal year, executive awards were compensated to an executive officer within a period beginning four business days before the filing of the mandatory reporting document (or the file concerning disclosures of company's material non-public information), and finishing one business day after the filing of the report, the company must provide each such award in a mandatory new tabular format[89]:

- The name of the named executive officer
- The grant date of the award
- The number of securities underlying the award
- The per-share exercise price
- The grant date fair value of each award computed using the same methodology as used for registrant's financial statements under generally accepted accounting principles
- The percentage change in the market price of the underlying securities between the closing market price of the security one trading day prior to and one trading day following the disclosure of material non-public information

[88] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86 – page 88
[89] Final Rule: Insider Trading Arrangements and Related Disclosures, Securities and Exchange Commission, 17 CFR Parts 229, 232, 240, 249, Release Nos. 33-11138; 34-96492; File No. S7-20-21, RIN 3235-AM86 – page 103

The main purpose of this new provision's table is to highlight for investors options premium grants that could be more likely than most to have been made at a time that the company's board was aware of material non-public information affecting the value of the award.

3.3. Conclusions

Summarizing the main innovations and\or changes made by the SEC in the discipline relating to the regulation of insider trading and affirmative defense, we can see that the most revised topics were substantially:

- Insider trading companies' policies
- Requirements about the disclosure of material non-public information
- Corporate insiders bona-fide gifts
- Executive compensations\awards

As far as insider trading policies are concerned, what emerges from the new regulations is that substantially they must be updated with reference to the Effective Date, but that existing or scheduled and pre-declared trading plans with reference to February 27, 2023, may not be updated\modified if these do not involve changes to the so-called "Essential Terms" (grant date, exercise price, number of securities, …)

With these new changes, a certain will is perceived on the part of the SEC to want to strengthen the set of disciplines that can constitute corporate policies on the coordination of insider trading and disclosure of material non-public information so that, by February 27, 2023, all companies will have to re-update or reconsider their related policies in order to be in line with current laws and procedures to amend any provisions that conflict with the final rules.

One of the main issues to be reviewed is undoubtedly that relating to the cooling-off period, since the vast majority of listed companies, if not all, already provide for a cooling-off period for their corporate insiders but the duration of this period will probably have to be shortened\adapted to the provisions of the final rules. Moreover, companies could consider removing internal policy provisions requiring insiders to trade only through Rule 10b5-1 plans in light of the new regulation, which will require prior disclosure of the number of shares intended to purchase\sell under the plans.

According to some critics[90], this change could lead to a consequent market price reaction and become a topic of discussion in shareholder engagement causing an ambiguous effect on the use of these trading plans by insiders. It could also happen that, in addition to reviewing their internal policies, companies may encourage insiders to trade during the open window periods after pre-clearance from the company's counsel, especially with reference to the aforementioned sell-to-cover transactions. In addition, with the new requirement to file insider trading policies as an exhibit to the Form 10-K, they shall revisit their procedures and organizations to make sure they are structured enough.

As regard the issue of equity compensation awards in relation to releases of material non-public information, it is clear that companies should consider waiting at least two business days following such disclosure report before making executive compensations. This stems from the fact that the SEC's final rules seem tailor-made to combat the "spring-loading" phenomenon, in which equity grants are made immediately before any positive public material disclosure of the company is released. In this way, executives benefit from the share price due to the effect of the market which therefore evaluates the positive information received in the price (such as for example a significant quarterly earnings announcement). In reference to this, by coordinating the specific internal offices and the board committee, the companies could adjust or mitigate potential concerns by waiting at least two business days following such releases and then make equity awards scheduling regulatory files.

Finally, it is useful to add a further consideration regarding corporate insiders' gifts. As we noted in Chapter 1, it can be observed historically that the SEC has never expressed a real regime on liability of gifts under Section 10(b) even if, with the new provisions, it is important to understand that corporate insiders who are aware or in possession of material non-public information should proceed with caution when gifting company securities. This is because they could be liable if they gift securities when the material information had not yet been made public, even if they had prior knowledge, if they know that the recipient of this gift would have sold securities before the announcement. In general, there could be the case that companies decide to completely reformulate the part relating to how their insiders can carry out gifting transactions within their insider trading policies, above all by virtue of the fact that they could be in possession of non-public information that would benefit them in an ante-disclosure period.

[90] Gibson, Dunn & Cutcher LLP, SEC approves new insider trading rules, December 16, 2022

As it has been observed in this first part of the chapter, the main purpose of the new changes made by the US legislator is to recognize more in advance all possible insider trading actions based on the misuse of material non-public information through trading plans. Specifically, the SEC therefore attempted to complement the effects of the cooling-off period for corporate insiders through the certification requirement. Furthermore, the Commission appears to have intended such cooling-off periods to work in parallel with the new restrictions regarding the use of multiple overlapping plans under Rule 10b5-1 (c) in an attempt to prevent potentially opportunistic plan cancellations based on material non-public information.

Moreover, in general, affirmative defense is voluntary so if insiders find the conditions of this defense to be overly burdensome, they could elect not to rely on it. As a consequence, if migration of trading outside of the Rule 10b5-1 plans' regime results in an increase or no change in the incidence of insider trading, the benefits of the amendments may be attenuated or offset.

The natural reality-based consequence of these changes is that whether there is indeed a direct shift in the future between trading outside the Rule 10b5-1 plans and the actual amount of insider trading actions will only depend on the extent and efforts that companies will begin to implement with increasing strength and precision regarding new mechanisms or any changes made to their insider trading policies or ethical codes of conduct based on enforcement actions, legal responsibilities, minimum listing standards or minimum reputation requirements ethics/morals and any new corporate governance mechanism (with the main purpose of increasingly discouraging and disincentivising insider trading and abuse of material non-public information).

In details, the new provisions concerning the cooling-off period for officers and directors is expected to reduce incentives to enter or modify plans based on material non-public information by ensuring that trades under the plan are executed at prices that fully reflect the material information that was previously non-public. This is expected to substantially weaken corporate insiders' incentives to enter or modify Rule10b5-1 plans based on material non-public information and, in addition, the total length of the cooling-off period is expected to largely prevent officers and directors from profiting on unreleased earnings results for the quarter in which the plan is adopted as well as other types of material non-public information. Finally, o the extent that such material may be time-sensitive, the Securities and Exchange

Commission expects the cooling-off period to effectively discourage corporate insiders from adopting new or modified plans on the basis of that non-public material[91].

3.4. Regulatory changes in EU

As regards the regulation of insider trading in Europe and the latest changes relating to its specific regulations, we find in chronological order the European Directive 2019-2020 relating to the regulation of market abuse.

In particular, every Member State of the European Union had to adapt and update their national laws at the beginning of 2021 regarding some main themes:

- The scope of application of the Market Abuse regulations and related exemptions
- Substantial changes in "secondary" insider trading
- New regarding the confiscation of assets and criminal convictions

On 27 December, 2019, in fact, EU Directive 2019/2177[92] of the European Parliament and of the Council of 18 December 2019 was published in the Official Journal of the European Union, amending Directive 2009/138/EC, on the subject of access to and exercise of insurance and reinsurance (Solvency II), Directive 2014/65/EU, relating to markets in financial instruments, and Directive (EU) 2015/849, relating to the prevention of the use of the financial system for the purpose of money laundering or terrorism.

As far as insider trading is concerned, it is useful to focus mainly on the amendments to Directive 2014/65/EU. First of all, it is established that these provisions apply to investment firms, market operators and firms from third countries which provide investment services or carry out investment activities through the establishment of a branch in the EU, therefore we

[91] *Some evidence of the extent to which requiring a longer period of time between Rule 10b5-1 plan adoption and the first trade under the plan could prevent insider trading is presented in the WSJ analysis. It shows that shorter periods between plan adoption and the first sale were associated with more negative stock returns after sale, which implies that more insider trading occurs in cases of trading commencing closer to plan adoption*, ibidem at page 142

[92] (EU) Directive 2019/2177 of the European Parliament, 27.12.2019, L. 334/155

immediately find a substantial extension of the scope of application of the laws on insider trading and market abuse.

Two most important definitions relating to the regulatory regime are then updated and modified, namely the terms “management body” and “senior management”. Therefore, by “management body” the new European legislation intends to refer to any body of an investment firm, a market operator or a communication service provider, designated in accordance with the respective national laws of the member states, which is empowered to establish the entity’s strategic policies, objectives and overall direction, which oversees and monitors management decisions and includes individuals who effectively direct the entity’s business (for example, the board of directors, counsel of directors, compliance or legal office, …).

Subsequently, the term “senior management” means any individual who exercises an executive function within an investment firm, market operator or communications service provider and who is responsible for the day-to-day management entity and accountable to the management body (e.g. CEO, CFO, Executive Officers, …).

After reviewing the definitions of these terms, it is then useful to focus specifically on the changes made by (EU) Directive 2019/2177 on some very important aspects, mentioned at the beginning of the paragraph, to also understand what the major differences are currently compared to current legislation in the United States.

3.4.1. Scope of application of Market Abuse regulation

The European legislator has therefore extended the scope of application of the discipline, as well as the cases of exemption, but at the same time has also proceeded to a more modern systematic reorganization of the relative rules and articles.

In particular, the article concerning the rule that governs the application regime of the provisions on market abuse was modified, limiting the scope of the articles regarding:

- The abuse or the unlawful communication of material non-public information
- Recommending or inducing others to commit insider dealing
- Market manipulation

With these new "application extension" changes, the European Commission has provided that these provisions apply, in addition to the facts concerning the financial instruments admitted to trading, in a regulated market in a Member State, or in a multilateral trading system, the financial instruments traded on an organized trading facility, conducts or transactions relating to auctions on authorized platforms (such as a regulated market for emission allowances or other related auctioned products) even when such products are not financial instruments, the price or value of which depends on the price or value of the financial instruments set out in EU Directive 2014/65/EU, or has an effect on them (also including credit default swaps and differential contracts).

The latter category, unlike the others already included in the previous versions of the Directives[93], was therefore included in the provisions of the article in question as expressly provided by article 1 of the MAD II. Furthermore, it is established that the entire discipline concerning market manipulation must also be applied to events or phenomena concerning:

- Contracts on goods that are not wholesale energy products, capable of causing a significant effect of alteration\reduction in the price or value of the financial instruments mentioned above
- Financial instruments, including contracts on derivatives or the same derivative instruments for the transfer of credit risk, capable of causing significant effect of alteration\reduction in the price or value of contracts on commodities in the event that they depend on the price or the value of these financial instruments
- The reference indices, defined as benchmarks

The amendments to these articles, rather than introducing real substantial innovations with respect to the previous Directives, seem to be aimed at a general and systemic reorganization of the various and fragmented provisions on the scope of application within the same articles with a view to greater juridical robustness and systematic accuracy, taking the US regulatory structure as a reference model[94].

As regard the exemptions, the art. 26 (1-b) of the European Law 2019-2020 modified the cases of exemption from the application of the market abuse regulation, adding in details letter b-bis which establishes that this market abuse regime should not be applied to trading

[93] Directive 2014/65/EU, Directive 2016/1011/EU, Directive 2019/2115/EU
[94] Le principali modifiche della Legge Europea 2019-2020 alla disciplina del market abuse, February 8, 2022, A. Castorino, F. Mezzasalma

carried out for the stabilization of real estate values with reference to article 5 of the MAR concerning[95]:

- Transferable securities, i.e. shares and other transferable securities equivalent to shares, bonds or other forms of debt securities, debt instruments convertible or exchangeable into shares or other equivalent securities
- Related instruments, i.e. contracts or rights to subscribe, acquire or sell transferable securities (where the transferable securities are convertible or exchangeable debt instruments), the transferable securities in which the debt instruments may be converted\exchanged, instruments issued or guaranteed by the issuer or guarantor of the securities and whose market price may significantly influence their price, or shares represented by such securities as well as all other securities equivalent to such shares.

3.4.2. News on "secondary" insider trading

As regards the so-called secondary tipping or insider trading activity, a matter which was extensively discussed in the first two chapters especially with reference to the developed discipline in the US, Article 26 (1-c) of the European Law 2019-2020 has provided for a regulatory change as regards the new introduction of the crime of secondary insider trading, thus outlining a system based on the "cumulative double track", i.e. both in addition to the traditional sentence with administrative sanction, the criminal sanction in the strict sense was also added and flanked.

Historically in Europe, the evolution of the sanctioning discipline on inside trading and market abuse has always shown itself to be quite fluctuating as a long series of interventions have followed another aimed initially at the criminal repression of the conduct, then at their decriminalization, and finally again with additional criminal cues.

As seen in Chapter 1, the criminal law on secondary insiders was introduced for the first time in Europe in 1991 and subsequently modified and renewed following the changes promulgated with Directive 2003/6/EC (MAD I), which is therefore become punishable exclusively by administrative means. Finally, with the MAD II, we can see in Europe the return of the phenomenon of secondary insider trading, deriving directly from the same rules applied to the classic corporate primary insider trading. The main aim of the European Commission therefore seems to be to promote a greater dissuasive effect on potential offenders through the tightening of new criminal penalties for market abuse.

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[95] (EU) Directive 2019/2177

In a very similar way therefore, as we could see with the new provisions on insider trading in the US at the beginning of the chapter, both the European and US legislators have tried to undertake a more rigorous and much broader treatment (in terms of regulatory application) against transgressors, defining their behaviour as unacceptable due both to their responsibilities towards companies but above all due to the potential negative repercussions that are unequivocally reflected on the market and on the confidence of investors and markets.

To outline a more precise picture regarding sanctions in the regime of insider trading in Europe according to the double track mentioned above, we find[96]:

- For secondary insiders: administrative sanction with a pecuniary fine from 20.000 to 2.500.000 euros, criminal sanction of imprisonment from 1 year and 6 months to 10 years
- For primary insiders: administrative sanction with a pecuniary fine from 20.000 to 3.000.000 euros, criminal sanction of imprisonment from 2 years to 12 years

Moreover, it is interesting to point out that in both situations of crime the pecuniary penalty can be increased up to three times or a greater amount of ten times the product or profit obtained from the crime when, due to the relevant seriousness and offensiveness or recurrence of the crime, for the personal qualities of the perpetrator or for the entity of the product\profit achieved.

In addition, in a very similar way to the US regulations, these administrative and penal sanctions are added to the ancillary sanctions such as for example the temporary or definitive disqualification from carrying out administrative, management and control functions with the subjects authorized pursuant to the European Directives or the listed companies (see in this sense the final sanctions envisaged for corporate insiders of Netflix and for Elon Musk with Tesla, Chapter 2).

3.4.3. New provisions about preventive confiscation

Finally, it also useful to underline the last main issue subject to new changes in the regime of insider trading in Europe: the preventive confiscation. In accordance with the provisions of

[96] EU Directive 2014/65/UE

EU Directive 2019/2177, the article concerning the confiscation of assets which constitute the profit of the offense but no longer also the product of this offense has been replaced[97].

In the section which provided for the compulsory confiscation, direct or by equivalent, of the product of the crime (i.e. the total value of the financial instruments purchased or of the proceeds from the sale of the same) and of the assets used to commit it (i.e. the sums invested in the purchase or alienated instruments), and not just the profit itself (i.e. the economic utility realized through the insider trading operation).

The European Commission has therefore decided to revise this provision since the judicial body has deemed it appropriate to observe that the mere confiscation of the profit derived from the crime has a purely restorative nature, unlike instead the confiscation of the product of the offense which has a substantially punitive nature, create a sort of disproportion between the final sanctioning responses.

3.5. Comparing US and EU Regulations

In light of what has been analysed up to now, it is possible to establish some objective reflections regarding the final conclusions on the main substantial regulatory differences as regards the regulation of insider trading in the US and EU.

The first fact to be analysed is undoubtedly the American starting point in the matter of prohibition based on the violation of a fiduciary duty (even if, as we have seen, with some exceptions in some cases), while the approach of the European legislator seems to embrace the general concept of equal access to information. The US reliance on breaches of fiduciary duties has been adopted to limit the potentially very broad reach of the equal access to information approach.

Consequently, this different legislative approach is inevitably reflected also in the context of disclosure obligations of reporting corporations. In fact, in the US legislation we do not find a general duty to disclose all material information similar to the corresponding European rule (based, as mentioned, precisely on the cardinal principle of equal access to information).

What follows therefore is the fact that, as argued in the first two chapters, the American regulatory architecture seems in some way substantially fragmented and sometimes contradictory or inconsistent within a regulatory system in which the plaintiff must generally

[97] Le principali modifiche della Legge Europea 2019-2020 alla disciplina del market abuse, February 8, 2022, A. Castorino, F. Mezzasalma, page 6

be able to establish the existence of a fiduciary duty and the fact that it has been in some way breached.

On the other hand, European legislation, despite having always taken the American legislative system as an example to follow and a reference model, is broader and enforcement actions are not necessarily obliged to undertake the same legal loopholes regarding fiduciary duties to successfully argue a violation of insider trading prohibition.

Despite these substantial "philosophical deviations" of thinking and promulgation of laws, when we look at the practical implications of US and EU rules, with respect to the scope of application of insider trading, the two systems are very similar. There are and will always be, obviously, situations and cases in which European laws would apply, but American ones would not, or vice versa, but they are fairly limited, and they concern only the tipping activity or secondary insider trading[98].

With regard to this last consideration, it is useful to specify that the major difference that can significantly be noted at a regulatory level concerns the burden of the proof, since in the United States in most cases it is necessary to demonstrate, and therefore find sufficient evidence, to a breach of a fiduciary duty and, in the specific case of tippees, the awareness of such breach. On the other hand, another notable difference between the two legal systems is that in Europe we do not find laws or provisions similar to Section 16(b) of the American Exchange Act. In fact, this particular section of the law empowers US investors with an effective tool to sanction the most possible insider trading violations especially with regard to primary corporate insiders through private litigation. Unlike this, public enforcement is the most commonly available tool in European countries to be able to promulgate the final sentences of conviction against criminals[99].

As far as the enforcement of insider trading prohibition is concerned, it is useful to underline that there are different channels and sanctioning methods available to the European and American legal bodies.

First, in America the Securities and Exchange Commission can bring administrative actions against insiders, but, in addition, it can seek help or use another ancillary tool through the opinion of the federal courts and defer alleged violation to the Department of Justice for criminal prosecution.

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[98] MPILux Working Paper 5, Comparing Insider Trading in the United States and in The European Union: History and Recent Developments, 2014

[99] Ibidem at section 4.1. Comparing Substantive Provisions: U.S. vs. the European Union

Furthermore, private plaintiffs also have the possibility of bringing a complaint against insiders through Section 16 (b), rather than the actual Rule 10b-5, in the light of the lower burden of the proof provided by the former. In any case, the main reason for the greater prevalence of public enforcement in the US is that insider trading, especially in cases based on Rule 10b-5, is very difficult to prove. The simple discovery of the crime on the basis of the tools available to private individuals are not, in legal reality, sufficient enough to form an effective and undoubtedly recognized evidence at the regulatory level, while the SEC and the attorney general obviously have more extensive investigative powers.

A further distinctive feature of the discipline regarding insider trading and market abuse in the US is its complex judicial structure, i.e., violations of this law can be prosecuted both at the level of administrative and criminal sanctions, but also at the level of penalties and sanctions private. This fact naturally derives from the enforcement procedure of convictions and complaints, since in principle enforcement actions can be brought by the Securities and Exchange Commission, the Department of Justice, and private litigants. This type of judicial structure is actually also present in Europe, where in many national legislations of the Member States they provide for both criminal and administrative sanctioning consequences, but also private causes of action are also available (as for example in Italy, Germany and UK).

Recent studies have then brought to light a debate that has always been very heated regarding the fact that in America, according to the data reported by some reports, the prosecuting insider trading actions are much higher than in Europe with a disproportion at a first sight very remarkable (for example in the US between 2001 and 2007 over 300 insider trading actions were carried out against 600 individuals or entities, while in the same period there were only 8 cases of convictions in the UK, 3 cases in Italy and 12 in Germany)[100].

Although the empirical data show that in absolute terms there seems to be a big difference in the effectiveness of American law compared to European law, if we focus on the relative data, this perspective does not seem so real. In fact, it is not possible to forget in this analysis that, as extensively analysed also in Chapter 1, other factors must always be taken into consideration, such as the effective dimensions of the different European national markets compared to the American one, both in terms of the number of reporting corporations and of market capitalization.

[100] Ibidem at section 4.2. Public and Private Enforcement of Insider Trading in the US and Europe

The data which most reflects these substantial differences is the number of listed companies in the US, approximately 5500, compared to the European ones at a national level (for example in Italy the number of listed companies does not even reach 300).

In conclusion, it can be said that with respect to the discipline of insider trading, the US regulation has had both the advantages and disadvantages of being the pioneer of the entire legal regulation in the field of promulgation of laws. As mentioned, the US was the first country engaging in both public and private enforcement of insider trading mainly through two tools: Section 16(b) of the Exchange Act 1934 and Section 10(b) through Rule 10b-5.

We can state that the former is a real easily rule to apply and it is a helpful tool in discouraging the most egregious insider trading by primary insiders, even if it relies on a presumption of use of inside information.

Instead, Rule 10b-5 and the entirety of Section 10(b) are "anti-fraud" provisions characterized by a very broad scope of application even if they never specifically refer to the regulation of mere insider trading. Consequently, the insider trading enforcement regime is a normative derivation of these general provisions based on case law and administrative regulation enforcement by the SEC.

If, on the other hand, we look towards the European continent, we find a situation in which all the different Member States of the European Union have had to adapt their individual national legislation on insider trading over time on the basis of the Directives of the European Council and the European Commission. However, they dealt with this discipline years later than the US, taking them as an example in a situation that we can define as a "late comer".

As we have seen in Chapter 1, regulation was enacted primarily through the use of Directives at the European level, trying to obtain as a result a sort of harmonization at a continental level among all different Member States. European rules tackle the issue of insider trading and market abuse more explicitly and directly than their overseas counterparts, therefore resulting in a more clear and systematic approach.

Moreover, we find another important systemic difference if we think that the American federal courts, and in particular the Supreme Court, have decided to base the prohibition of insider trading on the violation of fiduciary duties. This instrument of judicial principles has undoubtedly been used as a weapon to prevent the real objective of insider trading, and its possible effects on financial markets.

On the other hand, Europe has embraced the parity of information approach, which basically condemns any trading while in possession of private price-sensitive information[101]. In the general framework of a possible future harmonization of the two regulations, to try to obtain a single global legislation on insider trading, a statutory adoption in the US of the parity of information theory may not be impossible to achieve. However, this would involve a complete revolution and revision of all American regulation, which have with latest changes over the years slightly deviated from the fiduciary-duty-based theory especially through the misappropriation theory, and above all it would involve a general reorganization with important changes at the path-dependency level of the US legal system.

Notwithstanding the almost opposite underlying philosophies of insider trading and market abuse in the US and in Europe, from a practical point of view, one does not find such "dramatic" divergences regarding the common objective of application of the prohibition. Instead, what can inevitably be deduced from our analysis is that the real difference lies in how the two regulations approach about the demonstrative and investigative phase of conviction and final judgment against the transgressors of these laws and the relative different methodology in prosecuting insider trading crimes (which even in recent years are higher in the US, but in Europe there is an increase in cases of prosecution of insider trading compared to early 2000s).

3.6. Social Media and Insider Trading

In the last section of this chapter, we will try to draw conclusions about what was analysed in Chapter 2 through specific cases of insider trading violations regarding Elon Musk and Netflix Insiders.

The first case show us how, although it is a widespread practice in the US to disclose or share important company information to its employees (such as the number of new Netflix subscribers to its data software engineers), there is no doubt that top management is in contact with this information on a daily basis through any activity carried out within the board of directors or on the basis of the roles obtained (just think of the control bodies, executives officers, board of directors, etc.). This information, despite its possible different nature such

[101] Research Handbook on Insider Trading, Stephen M. Bainbridge, University of California, 2014 section 1. The proposal for a directive on criminal sanctions for insider dealing and market abuse

as the announcement of a merger or the purchase of a company, or such as quarterly earnings announcements for example, is the most important material for a company as it is through such material that we could see the influence not only on the markets, through the price changes of its securities or derivatives, but also the global reputation in the eyes of external investors.

This material information therefore requires particular implicit protection: on the one hand, it is essential for the company's reputation and its economic and financial results, on the other, it must be protected against investors outside the company to preserve access only to corporate insiders but also to the public.

Moreover, information accessed by company employees and officers during service and employment is firm property. As we have seen, business ethics codes require corporate executives to keep material private information confidential and refrain from making trading profits based on this information. The use of private information that top executives acquire in their positions to engage in insider trading and to gain abnormal profits is in absolute violation of the widely accepted codes of business conduct (as seen regarding Netflix Insider Trading Policy and Tesla Code of Business Ethics) and thus is an ethical issue.

In a recent article on August 3, 2021, CEO Social Media Presence and Insider Trading Behaviour[102], the profile of a CEO that gains growing importance in today's business world (CEO social media presence, as we could observe for example through the behaviour of Elon Musk on Twitter concerning statements about Tesla) is outlined and it demonstrates how it is closely related to the ethical issue of insider trading.

In the article, it is empirically demonstrated how CEOs with social media presence are more likely to purchase their companies' stocks, to conduct such buys with a higher intensity and to derive greater trading profits from these trades.

Moreover, these purchases are opportunistic in nature and do not adhere to any standard routine scheme or patterns. The results of this article lead to the conclusion that social media presence affects insider trading through the channel of CEOs' private information. This conclusion does not seem to be all that unexpected if we consider that in recent years, after the explosive development of social networks and social media, corporate executive officers with higher social presence are more likely to engage in unethical indulgent behaviour such as

[102] CEO Social Media Presence and Insider Trading Behaviour, JOUR, Li, Frank et al, SSRN Electronic Journal, August 3, 2021

abusing their inside material information advantage and profiting from trading their companies' stocks.

In the specific case of Elon Musk, a recent 2021 study, The Effect Of Social Media Activity On The Market – Case Elon Musk, Evidence From The US[103], attempted to empirically analyse Elon Musk's Twitter activity trying to find a relationship between his tweets and the rates of Tesla and some crypto currencies.

According to the results of this study, Elon Musk's tweets do not have a massive impact on the specific asset values in the article but there are only statistically significant data in the case of Tesla. In fact, the values of the cumulative abnormal returns seem to contradict the efficient market conditions, indicating a deferred investor reaction over time starting from the event declared by Elon Musk on his profile.

In conclusion, despite the new European Directives and the new provisions made by the American legislator in 2022 regarding insider trading and market abuse, there still seems to be a regulatory vacuum or at least a grey area regarding the possible prohibition or control by the supervisory about declarations of top managers\CEOs through the use of social media such as Twitter, Facebook or Instagram.

In today's world, many official profiles on these platforms are undoubtedly on a par with characters defined as "influencer", with a following of millions people and with an out of the ordinary media importance. This ever-increasing popularity on the part of CEOs entails an inevitable possibility of using their profiles as a weapon of false or misleading statements in order to then be able to take advantage of them on the market though insider trading operation.

For future studies or research on this particular theme, it would also be useful to specifically analyse how the new US laws on corporate insider trading policies have actually been implemented by companies after February 2023, and how these have in practice adapted their codes to the new changes and whether, within these policies or codes of conduct, there are references to the use of social media.

In the future, it would be also desirable to enact a tailor-made law both at European and American level concerning the activity of public disclosure of material information on social channels through more stringent preventive supervision with the aim of primarily protecting

[103] The Effect Of Social Media Activity On The Market – Case Elon Musk, Evidence From The US, J. Kuokka, LUT University, Bachelor's Thesis, 2021

investors and the markets, and secondly the companies themselves, within the limits of the rights of freedom of expression of each individual.

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