IN THE PROCEEDINGS BEFORE THE ENFORCEMENT COMMITTEE ESTABLISHED IN TERMS OF SECTION 97 OF THE SECURITIES SERVICES ACT, 36 OF 2004

CASE NO: **12/2008**

In the matter of:

THE DIRECTORATE OF MARKET ABUSE	The Referring Party
and	
BROWN, MICHAEL JOSEPH IGNATIUS	First Respondent
McGREGOR, RORDEN	Second Respondent
CHEMINAIS, ANDRE DOMINIC	Third Respondent

DETERMINATION OF THE ENFORCEMENT COMMITTEE

Before The Hon Mr Justice C F Eloff, M R Johnston and J S M Henning.

CHAIRPERSON: I will now give reasons for our conclusion. This hearing was preceded by an investigation undertaken by the Directorate of Market Abuse of the Financial Services Board concerning the question whether any one or more of the three respondents contravened Section 73 of Act 36 of 2004 by insider trading.

It appears from the affidavit of Mr Van Deventer, the Executive Director of the Market Abuse Directorate, that after investigations of the matter, the DMA resolved to refer the matter to the Enforcement Committee. Then Act 22 of 2008 came into force with effect from 1 November 2008. It repealed the sections under which the DMA and the Enforcement Committee had been operating, but in Section 78(4) provision was made for transitory matters.

It is likely that by 1 November 2006 the actual referral to the Enforcement Committee had not yet taken place, although the investigations were ongoing. It is this circumstance which prompted the respondent's counsel to raise what is essentially a point *in limine.* The point was that the transitory provisions do not apply and that the investigations of the DMA had come to an end as at 1 November 2008.

I should incidentally observe that the repealing section of the 2008 Act did not bring about the demise of the Enforcement Committee. The Committee is kept very much alive, although in certain respects its composition has altered and different procedures are provided for.

After argument in regard to the point *in limine* was completed, the panel adjourned and then concluded that the point should be dismissed, reasons to be given later. Our reasons follow.

The issue is mainly one of the interpretation and meaning of Section 78(4) of the 2008 Act. It reads *"(4), the deletion by virtue of Section 33 of the Act of the definition of (Enforcement Committee), in Section 1 of the Security Services Act 2004 and the repeal of Sections 94(e), 67, 68 and 69 of this Act do not affect any proceedings of investigation instituted, fine to be imposed or the payment of a compensatory amount to be required by the Enforcement Committee referred to in that Act and which was pending at the date of coming into operation of this Act, and any such proceedings, investigation, fine or payment of a compensatory amount may be continued, instituted or enforced as if this Act had not been passed".*

It will be seen that the subsection does not mention a reference to the Enforcement Committee. What is preserved is *"any proceeding and/or investigation instituted ... which is pending as at 1 November 2008".* And the concluding phrase in this subsection states that *"any such proceeding or investigation may be continued, instituted or enforced as if this Act had not been passed".* Plainly what is preserved is the continuation of such proceedings and investigations.

The referral to the Enforcement Committee is a step in the continuation of the proceedings. The subsection in our analysis means that if any part of the proceedings undertaken by the Financial Services Board occurred before 1 November 2008, the repeal of the sections I referred to earlier does not affect that which has taken place in consequence of the investigation. For these reasons the point *in limine* was dismissed.

I now turn now to the merits of the application by the Directorate of Market Abuse. For ease of reference I shall refer to the respondents respectively as Brown, McGregor and Cheminais. These proceedings were preceded by the interrogation of the respondents and various other parties. The persons interrogated confirmed their statements under oath. The questions and answers were recorded and constitute part of the evidentiary material on which this panel will have to make a decision.

A charge was then filed against the respondents. The respondents thereafter each made an affidavit, dealing extensively with the issues and on what was recorded at the interrogation. It has, of course, to be considered carefully.

In our view the Directorate of Market Abuse carries the onus of establishing on a balance of probabilities that the respondents

contravened Section 73. Counsel for the respondents urged that proof has to be beyond reasonable doubt. We do not agree. This committee, many years ago, decided the contrary. Its decision was taken on appeal and the Appellate Tribunal found no fault with our decision on this point. In various subsequent hearings counsel appeared to recognise the correctness of this decision regarding onus.

This inquiry seems, to us, largely to involve consideration of what inferences and conclusions can be drawn from established facts and admissions made by the respondents. It is accordingly necessary to record what facts were established. By way of introduction, we note that the two listed public companies largely involved were Cape Empowerment Trust Limited ("CET") and Dynamic Cables RSA Limited ("Dynamic"). They were listed on the JSE. It was common cause that the JSE is a regulated market, as envisaged by Section 73 of the Act and both companies are listed securities. It was also common cause that at October/November 2008 CET held a 52.7% interest in Dynamic.

The witness, Shaun Rai, was the CEO of CET and a Director of Dynamic. Brown was at all relevant times a non-executive Director of Dynamic. CET held the majority shareholding in the company, Alexandra Security (Pty) Limited ("Security"). Cheminais was at all

relevant times the Managing Director and a 49% shareholder of Security. Shaun was a co-Director of Security. McGregor was at all relevant times the Financial Director and Company Secretary of CET and the Company Secretary of Dynamic. He was also a public officer of Alexandra Security.

Another company referred to in evidence was Grand Parade Investments Limited, a subsidiary of CET, which held the gaming interests, casinos etc, of the company.

Brown was at all relevant times a consultant at Lewer and Company (Pty) Limited ("Lewer"), a stock-broking firm, which has a large number of clients that held Dynamic shares. Brown represented the interests of those shareholders on the Board of Dynamic. Although Brown was not a Director of CET, he often attended its Board meetings and a Director of CET consulted him from time to time on issues affecting the group.

I now set out facts which emerged clearly from the papers. On or about 4 October 2006 CET commenced with negotiations pertaining to the repositioning of CET's gaming interests, which were to be sold to Dynamic. The rationale behind the repositioning was that Dynamic's listing on the JSE would enable investors to trade in CET's

gaming interests. The gaming interests were, up to that stage, held through Grand Parade Investment, GPI Limited.

On 19 October 2006 Dynamic and CET commenced with the drafting of the announcement, which contained the details of the repositioning. Mr Shaun Rai, the Chief Executive Officer of CET, and McGregor, were intimately involved in the preparation of the aforesaid announcement.

10 On 2 November 2006, at 11h27, Dynamic and CET published a joint statement through the Stock Exchange News Service (SENS). The companies announced that Dynamic would be repositioned so that it held only CET's gaming interests. In addition, CET was to purchase Dynamic's subsidiaries and increase its shareholding in the latter company. The announcement contained the expected financial effects arising from the repositioning. Those were very positive for both companies.

Prior to 2 November 2006 the details of the joint announcement
20 constituted inside information, as contemplated by Section 72 of the Act. Both Dynamic and the CET share prices increased on publication of the joint announcement.

I shall presently discuss the question of the extent of the knowledge of the individual respondents at the relevant times. I shall point out that in October 2006 Brown handled a number of trades in CET with clients of Lewer and that if he was an insider, he should not have done so. I shall set out the evidence that McGregor informed Cheminais of the prospective deal and that Cheminais thereafter purchased CET shares, but first a few words on the law.

The relevant portions of Section 73 read *"insider trading ... (1) ... (2), an insider who knows that he or she has inside information and who deals directly or indirectly or any person on the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it, commits an offence ... (3)(a), an insider who knows that he or she has inside information and discloses the inside information to another person, commits an offence ... (4), an insider who knows that he or she has inside information and who encourages or causes another person to deal ... in the securities listed on a regulated market to which the inside information relates or which are likely to be affected by it, commits an offence".*

And "insider" is defined as *"a person who has inside information".* "Inside information" is defined as *"...specific or precise information, which has not been made public and which (a) is obtained or beknown to an insider (b) if it were made public would be likely to*

have a material effect on the price of value of any security listed on a regulated market". I shall later discuss the practical implications of those provisions in the context of the facts of this case.

I now turn specifically to the case against respondent Brown. The essence of the charge against him was that while an insider, he, on 28 October 2006, handled the deals of purchases of CET shares. The main question in the circumstances of this case is as to the extent of the knowledge of Brown in regard to the deal at the stage when he, through Lewer, acted for a number of persons in the purchasing of CET shares. There was no effective challenge of the evidence that during the last week of September 2006 Shaun Rai informed Brown, who, it will be recalled, was a Director of Dynamic, about the idea of repositioning the gaming rights held by CET. Shaun wanted Brown's views about the idea. It will be recalled that Brown, a stockbroker, was on the Board of Dynamic because he represented a large group of investors who held Dynamic shares.

It's also relevant that the evidence was that Shaun and Brown communicated daily. It was also said by Brown that Shaun Rai knew that he had considerable experience in the financial services industry. He also mentions in his affidavit that various possibilities were raised in discussions with Shaun Rai. It seems to us to be probable that Shaun Rai would have told Brown about the proposed

deal in sufficient detail to get Brown to support the idea. He wished to get Brown's support.

As we understand the affidavit made by Brown, he disputes the allegation that he became an insider because (said he), he did not as at 28 October 2006 hear that a deal had been finally concluded or the details of shares to be transferred, at what prices. He states that the information given was of a general nature and that imparting knowledge of that sort would not have a material effect on the prices of shares in the market. He contends that the information given to him was neither specific nor precise within the meaning of Section 73.

I mentioned earlier that it was adequately established as fact that by the end of October 2008 there was finality in the discussions between CET on the probability of repositioning ongoing gaming rights. It was, as I said earlier also, clearly established that in the middle of October Shaun had instructed attorneys to prepare the necessary documentation and that finality had been achieved.

Brown knew well before 28 October 2006 that the discussions were ongoing. He knew what the rationale of the proposed deal was and what the deal entailed and what the financial benefits would be. He knew enough to get him to express his support for the idea. I quote

his evidence ... *"and Shaun Rai knew he could count on my vote for going that route".*

It appears to us to flow from these facts that in order for Brown to express a strong support for the deal under discussion, he must have acquired adequate knowledge and understanding of exactly what the deal under discussion entailed and what its basic components were. Inevitably it must at least be inferred that by the end of October Brown knew the proposed deal had an unquestionable chance of attaining reality and that there was no reason to think that it might not be concluded. No mention was made by any of the witnesses of any real problems in the way of attaining fruition in this regard.

It is relevant that in his interrogation Brown said ... *"I always said to them, Rai and the Executive Directors, look, if there are problems, I want to know about it. I know I'm non-executive and my neck is on the line as well. I want to know if there is a problem. So, Shaun has been very open with me".* The evidence was that no problems were at that stage mentioned to Brown.

It is in this general context important that during the first week in October 2006, as I mentioned earlier, Shaun Rai had already instructed the legal financial and corporate advisors to prepare the necessary documentation and offer technical guidance on the

proposed repositioning. On 4 October 2008 the group's attorneys, Hofmeyr, were consulted. They had to draft the legal documents. The final agreement was signed on 30 October 2006.

It appears to us to be highly likely that Shaun Rai, with whom Brown had frequent contact and whose advice and support were sought, would have informed Brown of the final developments just referred to.

Clearly there is the need to consider the issue of whether Brown's information and perception as at the end of October 2006 were "specific" and "precise" within the meaning of Section 73. The allegations made by Brown in his affidavit that he was at, the relevant time, not informed of the precise figures and values of shares involved does not assist him. That which he plainly knew as at the end of October, was at least that there were ongoing negotiations with an almost certainty of finalisation, to agree on a fundamental repositioning, which had adequate support and was promoted by Shaun Rai who held commanding positions in the companies involved, had every prospect of success and are both specific and definite.

Brown did not need to know all the *minutiae* or finer points of the deal to enable him to realise that a specific, precise event was under discussion and that a signed deal was likely to eventuate.

In his affidavit Brown also states that he did not think that he had inside information. This statement cannot be accepted. He was a businessman with many years of experience. The prohibition on insider trading is well known and well understood in the commercial world. There is also the evidence that when Cheminais approached Brown to do a purchase of CET shares, Brown contacted Shaun Rai and enquired whether Cheminais was not privy to inside information. If Brown could have thought that by reason of this relative limited knowledge he might be privy to inside information, so much more must he have realised that he, Brown, was surely privy to insider information.

Next we have to consider the question whether it was adequately proved that the information "if it were made public, would be likely to have a material effect on the price or value of any security listed on a regulated market". In our view that conclusion should be made. The evidence was that when the announcement on SENS was made, the market value of both shares was significantly improved. In his answering affidavit Brown endeavours to avoid the implications of this fact by stating that the statement was accompanied by an

explanation that the deal would be beneficial to both companies and that that might account for the appreciation in the share prices. This statement appears to us to be speculative. We hold that even without such comments the market would have reacted favourably to what was taking place in the boardrooms in October 2006. The probability is that the market would have considered that the proposed deal was contemplated because it was in the interest of both companies. It would have noted that the Boards of both companies were strongly in favour of the deal. The market would have taken note of the fact that both Brown and Shaun Rai were confident that the deal would benefit both companies. The fact that Brown dealt in CET shares at the end of October 2006 was not challenged.

In the result we hold that the contravention of Section 73(2) alleged against Brown was adequately established. His conduct places him squarely within the ambit of Section 73(2).

That brings us to the case against McGregor. The essence of the complaint was that while he, at the end of October 2008, was privy to inside information, he discussed that information with Cheminais. In his answering affidavit McGregor admits that he was privy to inside information. His version of the discussions alleged with Cheminais is that the latter, late in October 2008, asked for an

explanation of the fact that while they normally discussed the affairs of Alexandra regularly, that no longer took place. I mentioned earlier that Cheminais was a Director and McGregor the public officer and that they met on a weekly basis. So, that is McGregor's explanation of his informing Cheminais in the way alleged.

Counsel for the Directorate of Market Abuse stressed the fact that Cheminais was not involved in any of the processes leading to the CET/Dynamic deal. We consider, however, that it's clear that his company, Alexandria, was likely to be vitally affected by the proposed deal. If it eventuated, Alexandria would have a new parent holding company with a new type of activity. Alexandria had a significant interest in the new deal and as the Secretary of the company, McGregor had the duty to inform the Directorate of what was going on. On this basis the charge against McGregor was not established and he is acquitted of the charge.

Lastly, we have to deal with the question of Cheminais. The essence of the charge against him was that he contravened Section 73(3)(a) in that at the end of October 2006, while he was privy to inside information, he purchased 212 736 Dynamic shares and 55 865 CET shares. As to the facts, I've already recorded McGregor's version of what he conveyed to Cheminais. Cheminais did not dispute this,

except that he said that he had no recollection of it. We think that the version of McGregor is to be accepted.

The relevant factors established by the evidence appears to us to be that Cheminais opened a trading account with Lewer on 29 October 2006, that is, after the abovementioned disclosure. Prior to that day Cheminais had not traded in any listed securities. He purchased the Dynamic shares on 31 October and 1 November 2006. He purchased the CET shares on 1 November 2006. The purchases were concluded before the publication of the joint announcement. Consequently he was possessed, in our estimation, of inside information and that he must have known that he was privy to inside information.

We conclude that his explanation for venturing onto the stock exchange market, namely that he wanted to profit with equities as his brother had done, does not hold water. It is very probable and we accept as a fact that he did so because of what had been told to him by McGregor. That means there was adequate proof that Cheminais breached Section 73(1) and our finding is that his guilt on that has been established. That concludes our reasons.

CHAIRPERSON: I take it that in the light of this, parties will consider the question of an administrative penalty. You will no doubt require time to consider this. We'll adjourn for half an hour.

Adjournment

On resumption:

CHAIRPERSON: The panel has now to decide on an appropriate administrative penalty arising from the finding against the first and the third respondents. I find it convenient to deal firstly with the position of the first respondent, Brown. In regard to him there are a number of aggravating features. He occupied a position of trust. He was experienced and must have been aware of the consequences of what he was doing. It is a serious case.

We think that the message should be sent out to the commercial world that insider trading is serious and should be seen as such. The seriousness of his offence should be reflected in the penalty imposed. We have considered the personal factors urged by counsel. There are aggravating features as well. We think this is an appropriate case to apply the provision of Section 77, namely that the profit of R18 906.00 is to be added to the penalty amount of three times the profit, R56 718.00. This amounts to R75 624.00 and this panel fixes the administrative penalty in that amount. The First Respondent is ordered to pay R75 624.00.

The position of the third respondent, Cheminais, is different. His offence was limited in time and amount and his contravention is not anything as serious as that in regard to Mr Brown. The Directorate of Market Abuse suggests that the norm fixed by the Act should be applied. We think that to do so will be unnecessarily harsh and an appropriate administrative penalty in regard to Mr Cheminais is R50 000.00. He is ordered to pay that amount.

I turn to the question of the costs. The Committee has the power to direct the liability for costs, and we think the respondents should pay the costs. We think it's appropriate that since most of the time this inquiry was devoted to Brown, he should pay substantially more as a contribution to the costs, than Cheminais. We order that the costs of the proceedings, including the fees of the panel members, are to be paid as to three quarters by Brown and one quarter by Cheminais.

That concludes the proceedings. We express our thanks for the contributions made by the parties and the spirit in which it was done.

CHAIRPERSON

15 March 2010