

Appendix A: Good Governance Guide: No 3.2

Category: Ethics and responsible decision making

Subject: Issues to consider in developing or reviewing the policy on trading in company securities

Source: Chartered Secretaries Australia

It is considered **good governance** for the board of listed entities to review regularly the company's policy on trading in company securities. This Guide is intended to outline issues to consider when developing or reviewing a policy on trading in company securities. Irrespective of the terms of the policy, the policy should be subject at all times to the law on insider trading.

The policy should also always be tailored to the requirements of the company concerned. What is suitable for a small start-up company may be quite different from what is suitable for a large corporate group. It is important not to copy another company's policy but to address each of the matters noted below in order to develop a culture where trading in company securities and any constraints on such trading is understood and adhered to.

Legal and regulatory context

The Corporations Act prohibits 'insider trading' generally and the ASX Listing Rules require notification of directors' dealings. The policy should also make reference to the ASX Corporate Governance Council 'Recommendation 3.2: Companies should establish a policy concerning trading in company securities by directors, senior executives and employees, and disclose the policy or a summary of that policy' and the contents of 'Box 3.2: Suggestions for the contents of a trading policy'. Companies also need to consider the legal and regulatory regime in more than one jurisdiction if the company is dual-listed.

Purpose of a policy

The policy needs to explain how the company restricts trading in company securities that is in breach of:

- legal and regulatory requirements
- the company's policy.

The board, senior executives and other internal or external persons who have access to inside information relating directly or indirectly to the entity need to be clear as to the risks that the entity's policy is meant to address.

Issues to address in the policy

It is **good governance** for the trading policy to address:

The prohibition on insider trading

The policy should provide an explanation of the prohibition on insider trading, including:

- an accessible and non-legalistic explanation of what inside information is. There is a definition of 'material information' in the context of continuous disclosure in ASX Listing Rule 3.1 that can be helpful in providing examples of what might constitute 'inside information'
- examples of inside information
- a list of what would have a material impact on the price of the securities, including examples specific to the company.
- clarification that the prohibition is mandatory and not a matter of guidance
- an accessible and non-legalistic explanation of what sanctions apply to insider trading and what consequences attach to directors, executives and employees from the company's perspective if the policy is breached
- an explanation that the prohibition extends to trading in the securities of subsidiaries (particularly partly-owned and related companies)
- an explanation that the prohibition may also extend to trading in the securities of other companies, including suppliers and customers.

Directors' interests notification

The policy should provide an accessible explanation of the legal requirements on directors to:

- notify the market of any trading, whether in company securities or otherwise
- notify the market of a substantial shareholding (more than five per cent) or any change(s) in that shareholding
- update the company's register of directors' interests, which may be minuted at the next board meeting.

Clearance to deal procedures

The policy should include:

- clearance procedures for allowing trading in company securities, including information on who must be contacted within the company to provide such clearance, in what circumstances clearance will be supplied or denied; and forms of notification before trading takes place
- how many days are available for trading once clearance has been provided
- a list of who is caught by the company rules on trading in company securities, with clarity on how the policy applies beyond the employment contract to spouses, dependents and external consultants and advisers.

Awareness of and compliance with policy

The policy should include:

- information on how the company approaches the development of a culture of awareness of the policy, and the matters it covers, for example, induction when commencing with the company; and ongoing training
- who is responsible for providing training on issues relating to trading in company securities
- how the company ensures the policy is communicated to all persons subject to it (including those external to the company)
- confirmation that ASX, ASIC and governance advisers take an interest in whether or not companies are complying with their share trading policies

Style

Attention to the following matters will assist in clarifying the terms of the policy to those to whom it applies:

- a summary of the main issues dealt with in the policy
- a glossary, including a clear definition of dealing (note that a poor definition of dealing will render the policy ineffective) and securities
- a set of questions and answers (Q & As) in relation to company rules for trading in company securities
- a process chart setting out clearance procedures and opportunities for trading
- a link to the Board Charter and Code of Ethics
- the title of the person who needs to be contacted if there are any queries.

Consideration needs to be given to:

- whether stock lending is included in the definition of dealing
- whether directors and executives are able to undertake any form of short-term trading
- margin lending and disclosures to the company of such
- whether exemptions of any kind will apply and in what circumstances. Such circumstances should not extend beyond:
 - genuine hardship (a potential tax liability does not constitute genuine hardship)
 - a court order or similar requirementand will need to be approved by the board or the chairman; however, if an exemption for genuine hardship or a court order or similar does not apply, the policy must not be silent on the issue but must state that any exemption is at the chairman's discretion.

Restrictions on trading

Restrictions on trading in trading policies can be expressed as either black-out periods, or trading windows (see Good Governance Guide 3.1: Trading in company securities: summary of issues). Regardless of which approach is decided by the company, it is **good governance** to ensure that the company clarifies which restrictions on trading are in place. A policy that does not include either a trading windows or a black-out approach to restrictions will give rise to reputational risk, as the perception could arise that trading is permitted at certain times despite legal prohibitions on insider trading.

Trading windows

A policy based on trading windows can:

- provide an opportunity that would not otherwise become available for directors and executives to deal in company securities. As it is now not uncommon for corporate activity to occupy most of the year, it can become difficult to locate a period in which directors and executives can trade without the perception arising that insider trading is occurring. However, the policy must be clear on the length of time for which the trading window operates, what triggers are appropriate to allow the trading window to operate, and be mindful of the continuous disclosure obligations to keep the market informed of price-sensitive information at all times
- give rise to a misunderstanding that trading is permitted during trading windows despite legal prohibitions relating to insider trading. It is important, therefore, that the policy clarifies that trading windows provide a conditional lifting of a blanket prohibition rather than permission and that any such lifting of the prohibition is subject to clearance procedures.

Black-out periods

A policy based on black-out periods can:

- clarify that restrictions and protocols are in place to counter any suspicion of insider trading
- provide reasonable (and easily defended) periods from balance date to results release for full and half-year results (and maybe quarterly blackouts for companies that report quarterly)
- give rise to a misunderstanding that trading is permitted in the period leading up to a black-out period despite legal prohibitions relating to insider trading. It is important, therefore, that the policy clarifies that trading windows provide a conditional lifting of a blanket prohibition rather than permission and that any such lifting of the prohibition is subject to clearance procedures.

It is **good governance** to include the following black-out periods:

- if the company is involved in corporate transactions that might have a material impact on the share price
- the period following the close of books until at least one trading day after the release of results (to allow time for the market to digest the results).

There may be a black-out period imposed at any time without explanation to those affected.

It is **essential** that the policy clarify that, irrespective of whether trading occurs in a trading window or outside a black-out period, no trading can occur if it involves the use of inside information.

The restrictions on trading should also provide:

- a clear explanation of what constitutes an active trade and what constitutes a transaction that may be excluded from the policy, subject to the prohibition on insider trading (such a transaction is sometimes referred to as a passive trade, and includes bonus issues and participation in dividend reinvestment plans, director and executive share plans and employee share plans)
- a policy on hedging and an explanation of how the company prevents executives from dealing in unvested entitlements.

The company secretary

It is **good governance** for the company secretary to:

- ensure that any letter of appointment for directors includes a requirement that in addition to obtaining clearance the director immediately and where practical in advance notify the company secretary of any trading in company securities (see Listing Rule 3.19B). The letter should clarify that directors are obliged to notify the market of any trading in company securities under s205G of the Corporations Act (14 days) and Listing Rule 3.19A (5 days).
- set up a process for directors to advise the company of indirect interests, including their SRNs and HINs. Trustees may deal in securities in which a director has or is deemed to have an interest (for example, a family trust or outsourced superannuation fund), without the director making a decision to trade, but the director maintains the legal obligation to notify the market (whether the securities are company securities or otherwise). Alternatively, directors may hold shares through a broker, with the financial adviser controlling the holding, and the director again is not the person making the decision to trade
- set up an 'alert service' through the share registry, to notify the company of any changes in the number of company securities held by directors in any one or more of their holdings, whether directly or indirectly
- circulate all Appendix 3X (initial) or 3Y (change) announcements to all directors, so that the board as a whole is kept informed of all trading by directors
- implement a reminder system, for example via email or the company intranet to alert directors, executives and employees when trading windows and black-out periods open and close.