WILMERHALE

The Inside Scoop: What does Tabernula tell us about the future of criminal insider dealing enforcement in the UK?

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The high-profile insider trading prosecution dubbed "Operation Tabernula", brought by the Financial Conduct Authority ("**FCA**"), has this month secured two further convictions. After a 12-week trial, Martyn Dodgson and Andrew Hind were found guilty at Southwark Crown Court on 9 May, and were handed prison sentences of 4.5 years and 3.5 years respectively. Three others who stood trial were acquitted.

The recent trial represents only part of the FCA's sprawling investigation spanning more than eight years and 10.5 terabytes of storage space, and costing an estimated £14 million. The FCA had already secured three guilty pleas in separate strands of the investigation.

The FCA has been quick to label this a significant coup, and a clear vindication of the extraordinary costs and manpower involved in the investigation. It is true that the 4.5-year sentence received by Dodgson is the largest ever handed down in a UK insider trading case. However, it falls noticeably short of the seven year maximum sentence, and even shorter of insider dealing sentences in the US. How, then, does the outcome in Tabernula compare to the FCA's previous successes?

The FCA's history of prosecuting insider dealing

The Tabernula investigation, targeting for the first time people who could be described as true City types, represented a step up for a prosecutor that had been criticised for going after "low-hanging fruit". The FCA (then the FSA) secured its first criminal conviction for insider dealing in 2009. Solicitor Christopher McQuoid was found guilty of passing inside information on the proposed takeover of TTP Communications to his father-in-law, who then traded on the information to make a total of £50,000. Both were found guilty, and received eight-month sentences. Shortly afterwards, Matthew Uberoi and his father (who famously communicated using a code based on a Chinese takeaway menu) were convicted of twelve counts of insider trading and jailed for one year and two years respectively. Even at this nascent stage, the FSA was determined to prove its worth as a heavyweight criminal prosecutor; as CEO in March 2009, Hector Sants made his intentions clear in announcing that the market should be "*very frightened of the FSA*".

Despite the tough talk, the FSA's enforcement record in subsequent years was mixed. It was particularly difficult for the FSA to escape unfavourable comparisons with its prosecuting counterparts across the Atlantic. In 2008, former Credit Suisse investment banker Muhammed Naseem was sentenced in the US to ten years in prison for insider trading. Michael J. Garcia, then US Attorney for the Southern District of New York declared that insider trading needed to be deterred by a “robust” sentence. While the higher sentence in New York was arguably commensurate with the level of financial gain involved—Naseem and his associate netted at least $7.8 million from their trades—the FSA’s successes paled in comparison to the formidable investigatory power of the US Department of Justice (“**DoJ**”).

By the end of the 2011 / 2012 financial year, the FSA had secured just 11 convictions for insider dealing, out of a total of 30 indictments. In the years that followed, under the stewardship of Martin Wheatley, the number of convictions more than doubled, with a total of 16 further convictions by the end of the 2014 / 2015 financial year. This was in large part due to the FCA’s increasingly sophisticated investigation techniques, which enabled it to take on a larger number of more complex cases. For example, print room investigation “Operation Saturn” spanned over four years, and included extensive use of forensic technology. Seven of the eight individuals charged in Operation Saturn were convicted, and received custodial sentences. FCA investigations were no longer confined to the UK alone: the trial of James Sanders and James Swallow, co-directors of brokerage firm Blue Index, along with Sanders’ wife Miranda, saw the FSA’s first cross-jurisdiction prosecution of insider dealing. This involved a parallel investigation by FSA, the US Securities and Exchange Commission (“**SEC**”), the DoJ, and the Federal Bureau of Investigation (“**FBI**”). James Sanders was sentenced to a record four years in custody, while Miranda Sanders and James Swallow were both sentenced to ten months in custody.

Where next for the FCA?

The successful convictions of Dodgson and Hind bring the tally of insider dealing convictions to 30. So far, the FCA’s enthusiasm shows no sign of waning; according to Mark Steward, Director of Enforcement and Market Oversight, “*[i]nsider dealing is ever more detectable and provable… lengthy terms of imprisonment, not profits, are the real result*”. Despite this apparent momentum, comparisons are once again being drawn with equivalent cases in the United States. In terms of headline-grabbing sentences for individual white collar offences, the United States has positioned itself at the head of the global race. After all, in 2011, hedge fund founder Raj Rajaratnam was sentenced to 11 years in prison in the United States on 14 counts relating to insider dealing. A year later, the sentencing record was broken again when Matthew Kluger, a lawyer at the Washington office of Wilson Sonsini Goodrich & Rosati who fed merger tips to a trader, was sentenced to 12 years in prison.

Given the increasing severity of sentences meted out to individual offenders in the United States in the post-crisis era, some believe it is inevitable that the UK courts will follow suit. Certainly the UK is ahead of the curve in Europe, and already exceeds the minimum sentencing standards set out in the new EU Directive on Criminal Sanctions for Market Abuse (2014/57/EU) (“**CSMAD**”) (and has thus opted out of CSMAD). The Fair and Effective Markets Review conducted by the Bank of England in 2015 recommends that the UK take even more stringent measures, by increasing the maximum sentence for criminal market abuse from seven to ten years' imprisonment, in line with other economic offences such as bribery.

However, we must not forget that to date, no criminal market abuse case in the UK has been tried which has resulted in a sentence being imposed at the maximum level of seven years—or even anywhere close. This could be read as an indication that there is little appetite in the UK courts for the level of sentences seen in the United States. The US sentencing model for economic crimes has itself come under criticism for being too rigidly tied to the total amount of money involved: for example, Kluger's 12-year sentence was calculated based not on the amount he received personally from the conspiracy (less than $1 million), but on the $35 million made by the traders he tipped off. While the sentencing trend in the UK is certainly an upward one, this does not necessarily mean we should expect a flurry of sentences in the double digits in the future.