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1 hot issues

Insider Information

When **insiders** of publicly listed companies, under Canadian securities law – specifically National Instrument 55-102 (NI 55-102), make changes in their shareholdings, they must be report them within 10 calendar days on the national publicly available database called **SEDI**[®] (“System for Electronic Disclosure by Insiders”) available on the web at www.sedi.ca. SEDI refers to the on-line computer system which is mandated by the Canadian Securities Administrators (CSA) and operated by the Canadian Depository for Securities (CDS).

The definition of an “**insider**” includes CEO’s, CFO’s, other company officers and directors. Shareholders who own 10% or more of company securities are usually also considered insiders. For background information on the definition of insiders and insider reporting obligations, refer to Canadian Security Administrators – Staff Notice 55-308. There are a number of exceptions to insider reporting obligations. In particular, some employee stock plan purchases can be exempted (NI 55-101) from the 10 day reporting rule. Also, issuers who buy back their own shares under a normal course issuer bid may file within 10 days of the end of the month in which the acquisition occurred. In addition, there are exemptions available for certain significant holders through NI 62-103. Going forward, it is expected that insider reporting rules will be revised when security regulators finalize proposed National Instrument 55-104 which is currently under consideration.

Anyone can view the insider’s profiles on-line on the www.sedi.ca site in the **Public Documents** tab. Under “View Insider Information”, insiders can enter their name or search by the company’s Issuer Number to locate their personal SEDI Profile.

Insider reporting obligations are comprehensive. Some of the more common types of transactions that require insiders to make a SEDI filing include when they:

- Purchase or sell shares
- Grant or exercise of stock options or receipt a stock dividend
- Expiration of stock options
- Transfer ownership of shares to another person
- Acquire ownership of more than 10% of the voting rights in a company or class of shares in Quebec (must also file an Early Warning Report on SEDAR)

There is also a Canadian company called INK Research (www.inkresearch.com) that puts the SEDI data to work for investors in a user friendly format. “**INK**” stands for **Insider News and Knowledge**. Through its Canadian Insider Alert Interactive service, INK highlights stocks daily that have insider activity which may signal opportunity or risk in the market place. They also provide filings search, charts, sentiment analysis and email alerts that notify subscribers if insider activity has taken place among any company on the user’s watch list. INK also offers a free website called **Canadian Insider**. The Canadian Insider link is canadianinsider.com. Users just insert the issuer’s ticker and they are able to view the last 10 insider trades by company. If users would like more information such as insider holdings as reported in SEDI, you can purchase a PDF for a fee. Canadianinsider.com also provides a helpful list of which Canadian reporting issuers have had recent insider filings.

Here are some Q and A's regarding insider trading (re-printed with the permission of INK Research):

Is Insider Trading Legal?

Company insiders have the right to buy and sell securities in their own firm so long as they are complying with securities laws and rules. This means, for example, that they cannot trade in their own securities when they are in possession of "material" non-public information, such as a pending take-over bid.

Are insider-trading reports new?

Until June 2003, insider reports were only available through each provincial securities commission. Now the national data base SEDI centrally collects all insider trading reports for most publicly listed securities in Canada.

I can't find a company on the SEDI system, why not?

If the company only reports in the United States, its insider filings may be filed with the Securities and Exchange Commission (www.sec.gov).

Why are insider-trading reports important?

Academic studies using US data suggest that corporate insiders may earn above normal profits on their trades (For example, see Lakonishok and Lee, Are Insider Trades Informative?, the Review of Financial Studies, spring 2001). The findings suggest that company insiders, as a group, may be better informed than the average investor about the prospects for their respective firms. However, there is no guarantee that similar results apply in Canada.

Should I as an investor simply do what the insiders do?

While insider activity can be an important screen and a potential indicator of a company's prospects, it is not a stand alone indicator. It is important to keep in mind that academic research has shown that following insider buying signals in isolation can result in holding stocks with both losses and gains. In the past, a few "big wins" among stocks with insider buying has been shown to compensate for the inevitable number of stocks that still go down despite insider buying. It is best to use insider trading data to identify potentially profitable trading ideas by incorporating insider signals into an overall portfolio strategy and due diligence process. We recommend that insider trading data be used in an investment process that considers a range of elements such as company fundamentals, sentiment and technical analysis. Fortunately, insider signals can be used by either contrarian (value) or momentum (growth) investors

Where can I read more about insider trading and stock returns?

Books:

- Jonathan Moreland, Profit From Legal Insider Trading, Dearborn Financial Publishing, 2000
- H. Nejat Seyhun, Investing Intelligence from Insider Trading, The MIT Press, 1998
- Tom Taulli, The Edgar® Online Guide to Decoding Financial Statements, Chapter 11, J. Ross Publishing

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