International Journal of Research in Social Sciences
Vol. 8 Issue 6, June 2018,
ISSN: 2249-2496 Impact Factor: 7.081
Journal Homepage: http://www.ijmra.us, Email: editorijmie@gmail.com
Double-Blind Peer Reviewed Refereed Open Access International Journal - Included in the International Serial Directories Indexed & Listed at: Ulrich's Periodicals Directory ©, U.S.A., Open J-Gage as well as in Cabell's Directories of Publishing Opportunities, U.S.A

CONFLICTING APPROACHES TO CAUSATION AND LOSS FOR NON-DISCLOSURE AND MISREPRESENTATION IN DISCLOSURE DOCUMENTS IN ZAMBIA—A CASE FOR THE FRAUD ON THE MARKET APPROACH

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ABSTRACT

Regulatory rules are likely to be violated if they are perceived to be weak or if enforcement is lax. Investors, in investing in securities markets, bank on the integrity of the regulatory framework and the market which integrity, in turn, depends on effective civil and criminal enforcement of regulatory rules.The study employs the doctrinal approach to evaluating legal rules. The main findings of the study were that:(1)the legal framework for public distribution of securities does not provide for a uniform approach to causation and loss for misrepresentation or omissions or pure non-disclosure in prospectuses and other disclosure documents, (a) with regard to prospectuses, the common law approach which requires proof of reliance—the causal link between the misleading statement and the plaintiff's loss—has been adopted (i) An argument has been made that, such a procedural requirement poses problems for investors in securities markets in the event that the loss suffered is caused by partial disclosure or pure non-disclosure. In such cases, it is obvious that the plaintiff investor will find it practically impossible to prove reliance since they cannot rely on undisclosed facts. Such a procedural shortcoming is likely to discourage participation of investors in new issues of securities in primary markets where prospectuses are traditionally used. (b) with regard to other disclosure documents than prospectuses, the statutory regime adopts a stricter form of fraud on the market theory (i) An argument has been made in this respect that absent a rebuttable presumption of reliance, liability of the offenders would be unrestricted; this is also likely to lead to unrestricted litigation (2)there is no policy justification for the different approaches to causation and loss for misrepresentation, omissions or pure-non-disclosure in prospectuses or other disclosure documents. Necessary proposals for reform as a possible way of remedying the shortcomings in the legal framework have been made.

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I

1. INTRODUCTION

This article sets out to establish whether or not the legal framework for public distribution of securitieshas provided adequate incentives for effective regulation disclosure-related fraud and pure non-disclosure and ensuring efficiency in securities markets in Zambia. The article evaluates the approaches to causation and loss for misstatements in disclosure documents and non-disclosure that are available under the Zambian legal framework and recommends the approach which is more suitable for the Zambian securities markets. An argument is made that given the small size and shallowness of the Zambian securities market, the 'fraud on the market' approach to causation and loss for misstatements in disclosure documents is likely to ensure fairness and efficiency in securities markets—a regulatory goal which is at the core of the Securities Act 2016.

1.1.MEANING OF 'MISREPRESENTATION'

Misrepresentation could either take the form of entirely false statements or half-truths. Thus, 'misrepresentation' means:-

a) an untrue statement of a material fact; or

b) an omission to state a material fact that is required to be stated or is necessary to prevent a statement that is made from being false or misleading in the circumstances in which it is made.[2]

Statements referred to in paragraph (a) above are 'the entirely-false' ones while those referred to in paragraph (b) are the half-truths—which is to say 'statements which are true in their own light but which when viewed in light of the undisclosed facts are rendered false.[3]

A fact is material if it significantly affects or could reasonably be expected to significantly affect the market price or value of the securities of the issuer.[4]However, it need not be the only inducement to subscribe for securities.[5]For purposes of establishing whether a statement is material or not, a statement must be construed in the natural and reasonable sense in which other persons are likely to read it.[6]

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[2] Definition of the term in section 2 of the Zambian Securities Act 2016
[3] *Suppressioveri* amounting to *suggestiofalsi*
[4] See, definition of 'material fact' in section 2 of the Zambian Securities Act 2016
[5] *Edgingtonvs Fitzmaurice (1885) 29 Ch D 459, Court of Appeal*
[6] *Smith vs Chadwick (1884) 9 App Cas 187, House of Lords*

II

2.BACKGROUNG TO THE PROBLEM

Civil recovery of loss occasioned by misrepresentations in prospectuses has its origin in common law actions of deceit. In cases of deceit it is necessary for the plaintiff to prove to the satisfaction of the court on a balance of probabilities that it is the misrepresentation of the defendant that caused his or her loss. Proving reliance establishes the causal link between the plaintiff's loss and the defendant tortious act. Obviously, such a procedural demand poses problems for investors in securities markets in the event that the loss suffered is caused by partial disclosure or pure non-disclosure. In such cases, it is obvious that the plaintiff investor will find it practically impossible to prove reliance since they cannot rely on undisclosed facts. Such a procedural shortcoming is likely to discourage participation of investors in new issues of securities in primary markets where prospectuses are traditionally used. Since investor participation creates demand for securities, such a negative feature in the law is likely to compromise liquidity of the securities market which is critical to the growth of the market.

2.1.STATEMENT OF THE PROBLEM

In light of the background to the problem under investigation given above, the statement of the problem may be formulated as follows:

"Has the legal framework for public distribution of securities provided adequate incentives for civil recovery, by investors, of loss occasioned by misrepresentations or omissions in prospectuses, or pure non-disclosure."

III

3.METHODOLOGY

This research falls into the qualitative research category. It focuses on answering specific questions relating to the problem under investigation by using both primary and secondary data. The research is underpinned by a doctrinal approach to evaluating legal rules. This method was used in analysing both primary and secondary data. Primary sources of data such as relevant legislation and case law touching on the subject/problem were used. Secondary sources such as journals and other written commentaries on primary sources were also used.

A checklist of documentary sources was used. The study employed non-probability sampling method in the selection of documents which were used in the analysis—purposive sampling. Both primary and secondary sources of data were used as aids to drawing inferences, making deductions and comparisons.

The main objective of the study is to answer the question whether or not the procedural legal framework for public distribution of securities has provided adequate incentives for civil recovery, by investors, of loss caused by misrepresentations or omissions in prospectuses, or pure non-disclosure. The study also sets out to flesh out some shortcoming in the regulatory framework currently in force and make necessary proposals for reform as a possible solution to those shortcomings.

The research questions used were:

a) Does the legal framework provide for a uniform approach to causation and loss for misrepresentation in prospectuses and other disclosure documents?

b) Is there policy justification for the approaches to causation and loss for misrepresentation in prospectuses and other disclosure documents?

c) Is loss caused by partial disclosure or pure non-disclosure in prospectusesrecoverable by investors?

IV

4.RESULTS OF THE STUDY

The results of the study may be summarised in tabular form as follows:

QUESTION	**ANSWER**	
	ZAMBIA	**UNITED STATES**
1. Does the legal framework provide for a uniform approach to causation and loss for misrepresentation in prospectuses and other disclosure documents?	NO	YES
2. Is there policy	NO	YES

justification for the approaches to causation and loss for misrepresentation in prospectuses and other disclosure documents?		
3. Is loss caused by partial disclosure or pure non-disclosure in prospectuses recoverable by investors?	NO	YES

2.CAUSATION OF LOSS FOR MISREPRESENTATION AND NON-DISCLOSURE

At common law, in an action for deceit, misrepresentation or indeed non-disclosure, it is not enough for the plaintiff to prove that they suffered loss. In order to succeed, the plaintiff must further prove that the loss incurred is as a direct result of the conduct of the defendant.

2.1.CAUSATION OF LOSS FOR MISREPRESENTATION IN PROSPECTUSES AND OTHER DISCLOSURE DOCUMENTS

In order for the plaintiff to succeed in an action for misrepresentation, the plaintiff must prove that their loss was caused by the misconduct of the defendant over and above proving that they have suffered injury. That way, they would in essence be establishing the necessary causal link between their injury and the defendant's misconduct. However, it must be noted that the necessity of proving injury and the requisite causal link between the injury and the defendant's conduct depends on the existence of a right of action to commence civil recovery actions. Absent such a right, no action can be commenced nor maintained against the defendant.[7] Consequently, the burden of proving injury and the necessary causal link between the injury and the defendant's misconduct does not fall onto the plaintiff. In this respect, it is necessary is to establish that a private right of action for civil recovery of loss exists. The following subsections look at this aspect.

[7] The maxim *'damnum sine locus standi'* which is literally Anglicised as *'damage suffered without the right to commence a recovery action'* applies here.

2.1.1.PRIVATE RIGHT OF ACTION FOR RECOVERY OF LOSS

The right to civil recovery of loss occasioned by misrepresentation is available for misrepresentation in prospectuses as well as misrepresentation carried in other disclosure documents than prospectuses.

2.1.1.1.A. PRIVATE RIGHT OF ACTION FOR MISREPRESENTATION IN PROSPECTUSES

Under the Zambian legal framework for the public distribution of securities, a purchaser of securitiesdistributed under a prospectus has a right of action for damages for any loss or damage sustained by reason of a misrepresentation in the prospectus.[8] Thus, an injured person may maintain a civil recovery action for damages against the following, namely:[9]

(i) the issuer or the securities holder, selling securities, onwhose behalf the distribution is made;

(ii) a person who is a director of the issuer at the time offiling of the prospectus;

(iii) a person who is authorised, or is named in, the prospectusas a director or as having agreed to become a director,either immediately or after a specified time;

(iv) where the issuer is not a reporting issuer prior to thedistribution, any person who was a promoter of the issuerwithin the twenty-four month period immediatelypreceding the date of filing of the prospectus;

(v) a person whose consent has been obtained to include arepresentation made by the person with respect to amisrepresentation in a prospectus derived from, or basedon, reports, opinions, valuations or statements that have been made by such person; and

(vi) any other person who signed a certificate in the prospectus,other than a person referred to in paragraphs (i) to (v).

B.SEC'S REPRESENTATIVE CIVIL ACTIONS

In addition to the private right of action on the part of investors and other market participants, there is SEC's power to commence representative civil actions for and on behalf of persons who may suffer loss as a result of misrepresentation in disclosure documents and pure non-disclosure

[8] Section 166(1) of the Zambian Securities Act 2016
[9] Section 166(1)(a)-(e) of the Zambian Securities Act 2016

resulting in misrepresentation. Consequently, with the underlying objective of dispelling the perception of laxity in the enforcement of regulatory rules for securities markets, the Zambian SEC has the right to bring representative civil actions in the name of, and on behalf of issuers and investors who have failed or are unable to commence action.[10] Thus, the SEC may, with leave of the High Court, bring such representative civil actions provided three conditions are met, namely:

(i) the Commission has reasonable grounds for believing that a cause of action exists under Part XV of the Securities Act 2016;

(ii) the issuer or securities holder has failed or is unable to commence an action; and

(iii) the Commission has given sixty days written notice to the issuer or securities holder who has refused or failed to commence an action;[11]

Where the perpetrator is sophisticated, small and medium scale issuers and individual investors may not have the same capacity as large scale issuers and institutional investors to get to the bottom of the activities of the perpetrator. Thus, the former category may not gather enough information about the activities of the perpetrator for the purpose of a case worth taking to the Capital Markets Tribunal. Geographical location and the biting cost of cross-border litigation may also work an added disadvantage to small and medium scale issuers and individual investors. Thus, such representative civil actions are heaven send for this category of issuers and investors.

In addition to the right to bring representative actions on behalf of issuers and investors, the SEC has also the right of intervention in cases where issuers and security holders do commence civil recovery actions.[12]This is exercisable in circumstances where the intervention of the SEC is necessary to realize the end of justice. For instance, documents and records relevant to the case of an injured issuer or investor may be in the custody of foreign branches of the respondent. In such cases, the applicant or plaintiff may not be possessed of adequate means to gather the required information. Thus, the intervening SEC could use its foreign relations with foreign

[10]Section 175(1) of the Zambian Securities Act 2016

[11] See, section 175(1)(a)(b)(c) of the Securities Act 2016

[12]Section 175(2) of the Zambian Securities Act 2016

regulators and request an investigation on its behalf. The foreign regulators may respond by invoking their power to act in support of foreign regulators and demand production of the relevant documents by those foreign branches of the respondent.

2.1.1.1.1.APPROACH TO CAUSATION OF LOSS FOR MISREPRESENTATION IN PROSPECTUSES

Critical to success of a civil recovery action for damages for misrepresentation is proof that the false statement was in the eyes of the law the cause of the plaintiff's loss. Reliance on the defendant's false statement by the plaintiff is said to provide the requisite nexus between the defendant's misconduct and the plaintiff's injury.

The Zambian Securities Act 2016 is silent on the approach which should be taken by courts in establishing the causal link between the defendants misconduct—the false statement—and the plaintiff's injury. That being the case, the English Common Law position serves as a complementary source.[13]

2.1.1.1.1.1.THE ENGLISH COMMON LAW APPROACH TO CAUSATION OF LOSS FOR MISREPRESENTATION IN PROSPECTUSES

The approach of courts to causation of loss occasioned by misrepresentation may be discussed under two heads, namely (i) entirely-untrue statements, and (ii) half-truths. The following subsection briefly discusses these categories, in turn.

A.APPROACH TO CAUSATION OF LOSS—ENTIRELY-UNTRUE STATEMENTS

English courts look to the causal link between the defendant's misconduct—issue of a false statement in a prospectus—and the plaintiff's injury—loss suffered by the plaintiff as a result of relying on the defendant's false statement. Thus, in order to succeed, the plaintiff is required to

[13] Subject the Zambian Constitution and subordinate legislation, the common law of England and rules of equity apply to Zambia: Section 2(a)(b) of the English Law (Extent of Application) Act, Chapter 11 of the Laws of Zambia. By 'common law' as used in the English Law (Extent of Application) Act, it is meant 'common law of England': See, definition of 'common law' in section 3 of the Interpretation and General Provisions Act, Chapter 2 of the Laws of Zambia. There is, however, an entrenched judicial practice to draw upon the wisdom of courts in other members of the Commonwealth which follow the English common law tradition such as, the United States of America, Australia, Canada and New Zealand.

plead and prove such reliance before the court. This legal position was reiterated by Lord Blackburn in Smith vs Chadwick, in the following terms:

"I think that if it is proved that the defendants with a view to induce the plaintiffto enter into a contract made a statement to the plaintiff of such a nature as would be likely to induce a person to enter into a contract, and it is proved that the plaintiff did enter into the contract, it is a fair inference of fact that he was induced to do so by the statement."[14]

Thus, effective proof of reliance consists in proving that:

(i) the defendant made the statement;

(ii) the statement was of such a character as is likely to induce a person to enter a contract; and

(iii) the plaintiff did in fact enter into the contract.

(i) Departure from Smith vs Chadwick?

As has been established above in England, the fact that a statement in a prospectus or other disclosure document is false does not ipso facto ground liability; the statement must also material in the sense of being capable of inducing persons to enter contract. Further, the plaintiff must actually enter a contract in relation to which the false statement is made. Thus, here 'materiality' consists in the capability of the statement to induce persons to enter contract. Similarly, in Zambia, the Securities Act 2016 requires something else over and above the statement being false. Consequently, it is required that the false statement be also 'material' not in the Chadwick sense but rather in the sense of significantly affecting or being likely to significantly affect the market price or value of the securities of the issuer. An argument is made that in this case, it would not matterthat the plaintiff actually relied on false statement if the court is of the opinion that it did not or is unlikely to significantly affect the value or price of securities of the issuer.[15] It is therefore submitted that the approach to causation of loss for misrepresentation in prospectuses under the Securities Act 2016 is a clear departure from Chadwick.

[14]*Smith vs Chadwick (1884) 9 App Cas 187, at 196*

[15] The plaintiff must also enter a contract for an action of misrepresentation to succeed. Misrepresentation is a contractual and not a tortious concept.

B. APPROACH TO CAUSATION OF LOSS—HALF-TRUTHS

There is no clear English authority on the approach to causation of loss for pure non-disclosure. For purposes of this article, we will draw upon the wisdom of other common law jurisdictions. The United States of America appears to have a well-settled position on this subject.

In the United States, Rule 10b-5(b) which was made under the Securities Exchange Act of 1934, is the equivalent of section 166(1) of the Zambian Securities Act 2016. Rule 10b-5(b) the United States Securities Exchange Rules 1942, provides that:

"It shall be unlawful for any person, directly or indirectly, by the use of anymeans or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange—

(b) 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;

….in connection with the purchase or sale of any security."

Existence of a Private Right of Action Under Rule 10b-5 of the United States Securities Exchange Rules 1942

Five years after the promulgation of Rule 10b-5, in Kardon v National Gypsum Co[16], it was held for the firsttime that r 10b-5 implied a private right of action so that investors who suffered loss as a result of a breach of that rule could sue those who caused their losses.[17]

Approach to CausationUnder Rule 10b-5—Early Case Law

How could one be said to rely on facts which have not been disclosed so that the requisite causal nexus between the conduct of the defendant and the plaintiff's injury could be said to have been met for purposes of liability?

Early case law in the United States required not so muchbelief in or reliance on the opposite of the undisclosed information, but rather look at 'whether the plaintiff would have been influenced

[16] 73 F Supp 798, 800, 802–3 (Kirkpatrick J)

[17] However, the Supreme Court of the United States did not formally acknowledge the existence of a private right of action until *Superintendent of Insurance of New York v Bankers Life & Casualty Co*, 404, US 6, 13(Douglas J)

to act differently had the defendant disclosed the undisclosed facts.'[18]In effect, this approach required that the plaintiff proves that he would have acted otherwise had he or she known the omitted facts—a burden quite too heavy to bear.

Approach to Causation Under Rule 10b-5—Later Case Law

Seven years down the line, the United States Supreme Court in the case of Affiliated Ute Citizensof Utah v United States[19]lightened the burden of proof in non-disclosure cases as established by earlier cases by streamlining the reliance test for non-disclosure cases. InAffiliated Ute Citizens, a bank and its employees purchased stocks from a group of American Indians in the latter's tribal company. The bank did not disclose the fact that those stocks were trading at a higher price in the secondary market with the aid of the bank itself.In an action for non-disclosure, the Court of Appeals for the Tenth Circuit rejected the plaintiffs' claim for damages and held that 'absent of proof of reliance on the defendant's fraudulent conduct by the plaintiffs, there could be no recovery under rule 10b-5.'[20] Dissatisfied with the decision of Court of Appeals for the Tenth Circuit, the plaintiffs appealed to the United States Supreme Court.On appeal, the Supreme Court reversed the decision of the lower court and held that:

"[P]roof of reliance on the nondisclosure was not necessary for recovery. Instead, where there is an obligation to disclose, the withholding of material information establishes 'the requisite element of causation in fact."[21]

The reasoning of the Court was that:

"Under the circumstances of the case—a case primarily involving a failure to disclose—positive proof of reliance is not a prerequisite to recovery. [All] that is necessary is that the facts withheld by the defendant be material in the sense that a reasonable investor might have considered them important in the making of the decision to invest.

The obligation to disclose and the withholding of a material fact establish the requisite element of causation in fact."[22]

[18]*List v Fashion Park Inc, 340 F 2d 457, 463, (2nd Cir, 1965),* (Waterman J)
[19] 406 US 128 (1972)
[20]*Affiliated Ute Citizens of State of Utah v United States*, 431 F 2d 1349 (10th Cir, 1972)
[21]Ibidem, pp. 153–154 (Blackmun J)

2.1.1.1.2.APPROACH TO CAUSATION OF LOSS FOR MISREPRESENTATION IN OTHER DISCLOSURE DOCUMENTS THAN PROSPECTUSES

Although section 167 of the Securities Act 2016 also confers a private right of action for civil recovery on persons who acquire or dispose of securities at a loss as does section 166 of the Securities Act 2016, it adopts a different approach to causation of loss for misrepresentation in other disclosure documents.

2.1.1.1.2.1. PRIVATE RIGHT OF ACTION FOR MISREPRESENTATION IN OTHER DOCUMENTS THAN PROSPECTUSES

The Zambian Securities Act 2016 confers a private right of action on any person who acquires or disposes of securities at an over-value or under-value, as the case may be. Thus, where an issuer or his/its authorized agent releases a document that contains a misrepresentation, any person who acquires or disposes of the issuer's securities, during the period between the time when the document was released and the time when the misrepresentation contained in the document was publicly corrected, **has, without regard to whether the person or company relied on the misrepresentation**[23], a right of action for damages against such an issuer.[24] In that case, the following may be sued alongside the issuer, namely:[25]

a) each director of the issuer of the securities at the time the document was released;

b) each officer of the issuer of the securities who authorised, permitted or acquiesced in the release of the document; and

c) each expert where—

(i) the misrepresentation is also contained in a report,statement or opinion made by the expert;

(ii) the document includes, summarises or quotes fromthe report, a statement or opinion of the expert; and

(iii) the document was released by a person or company, other than the expert, the expert consented, in writing, to the use of the report, statement or opinion in the document.

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[22]Ibidem

[23] This could only imply that non-reliance is not a bar to recovery of loss under section 167 of the Securities Act 2016. In a way, this approach sort of creates or imposes strict liability on market offenders.

[24] Section 167 of the Zambian Securities Act 2016

[25] Section 167(a)-(d) of the Zambian Securities Act 2016

2.1.1.1.2.2.APPROACH TO CAUSATION OF LOSS FOR MISREPRESENTATION IN OTHER DISCLOSURE DOCUMENTS THAN PROPSECTUSES

Section 167 of the Securities Act 2016 confers a private right of action on any person who suffers loss or damages as a result of acquiring or disposing of a security at a loss as a result of a misrepresentation in other disclosure documents than prospectuses, and this right of action is available **without regard to whether the person relied on the misrepresentation.** Therefore, section 167 of the Zambian Securities Act 2016 does away with the requirement of proving reliance before a civil recovery action for misrepresentation can succeed. It is therefore a sharp departure from the popularEnglish common law approach of requiring proof of reliance.[26] It is also a departure from the American, Australian and Canadian Fraud on the Market approaches which impose a 'rebuttable presumption' of reliance.

It is submitted that whereas a civil recovery action for misrepresentation under section 166 of the Securities Act 2016 depends on proof of reliance to succeed, the right of action under section 167 does not depend on such proof for success neither will a suit be defeated by non-reliance. These sections do set radically distinct approaches to causation of loss for misrepresentation in disclosure documents. But why should misrepresentation in a prospectus be treated any differently from misrepresentation in other disclosure documents? It is quite difficult to see any economic or other policy justification for such an approach.

In the absence of policy justifications for adopting two distinct approaches for regulating the same form of securities market misconduct, proposals are made for the adoption of either the Chadwick or the Basic Inc approach—fraud on the market approach—to causation of loss for misrepresentation in disclosure documents. In choosing the appropriate approach, regard must be had to the history, size and international character of the Zambian securities market and other markets in Eastern and Southern Africa.

[26] Australia has followed the English approach adopted in *Chadwick.*To this effect, Wilson J of the High Court of Australia in *Gould v Vaggelas* (1985) 157 CLR 215, has held that:. "If a material representation is made which is calculated to induce the representee to enter into a contract and that person in fact enters into the contract there arises a fair inference of fact that he was induced to do so by the representation.": at p. 236.

The Case of Non-Reporting Issuers—Un-Incorporated Issuers[27]

Section 167(1) does not include promoters in the list of person against whom a civil recovery action by an injured person may be commenced and maintained.Although the right of action is couched in general terms, the express mention of categories in respect of whom it may be exercised—directors, officers and experts—appears to effectively excluded categories such as promoters which have been left out.[28] It could be argued that a person who is injured by a misrepresentation in other disclosure documents filed by promoters has no right of recovery action under section 167 of the Securities Act 2016; that they have to look to the common law action of misrepresentation in which case they will have to prove reliance in the Chadwick sense.But why should other injured persons be subjected to a more stringent standard of proof than others in respect of the same misconduct? Yet again, there seems to be no policy or economic justification for such discrimination. As a possible solution to such inconsistence, proposals are made for the inclusion of promoters into the net of persons against who injured persons may maintain recovery action for loss or damage occasioned by misrepresentation in other disclosure documents than prospectuses.

2.1.1.1.2.2.1.PRESUMED RELIANCE OR TOTAL DISREGARD FOR RELIANCE?

In providing that the right of action is available to an injured persons**without regard to whether or not they have relied on the misrepresentation,** does the Zambian Securities Act 2016 impose presumed reliance or altogether do away with the requirement of proving reliance before an action can succeed?Having recourse to the tenor and spirit of the Ontario Securities Act in Canada could prove insightful with regard to the proper construction to place upon section 167 of the Zambian Securities Act 2016.

In an attempt to quell securities fraud and enhance market integrity, Canada has introduced statutory deemed reliance on the misrepresentation.In Canada, where a prospectus contains a misrepresentation, a purchaser who purchases a security offeredthereby during the period of

[27] 'Issuer' includes an un-incorporated entity which issues or proposes to issue securities during the pre-incorporation stage: See, the definition of 'issuer' in section 2 of the Securities Act 2016

[28] The Latin maxim *'expressiouniusestexclusioalterius',* applies. The maxim is Anglicized as *'express mention of a thing excludes all others'*. Since no illustrative words or terms such as 'includes' or 'such as' have not been used in section 167 of the Securities Act 2016 so such to suggest illustrative Parliamentary intendment, Parliament must be taken to have excluded all other categories not expressly mentioned.

distribution to the public shall be deemed to have relied on such a misrepresentation if it was a misrepresentation at the time of the purchase.[29] Injured persons have a right of action for damages against directors and various other specified persons.[30] Further in relation to take-overs, where a take-over bid circular sent to security holders or any notice of variation in respect thereof contains a misrepresentation, every security holder receiving the circular is deemed to have relied on the misrepresentation and may elect to exercise a right of action for rescission or damages against specified persons.[31] The courts in Canada have held that these sections impose a rebuttable presumption of reliance. The evidentiary burden of rebutting this presumption lies on the defendants.[32]

It is submitted that whereas the Ontario Securities Act presumes reliance, from the tenor and spirit of section 167, the Zambian Securities Act neither presumes reliance nor requires the plaintiff to prove such reliance. In effect, the Zambian Securities Act altogether does away with the requirement of proving reliance.It appear that all the injured person will need to succeed is to prove that the misrepresentation was of a material fact—that it significantly affected or was likely to affect the price of securities to which it relates. What may be said of such a state of affairs is the Zambian Securities Act embodies the efficient market hypothesis which requires efficient supply of information to the securities exchange so that the prices of securities reflect the true worth of the issuer and its securities. In effect, the Zambian Securities Act 2016 introduces the Fraud on the Market Approach to causation of loss for misrepresentation in its purest and harshest form and is consistent with economic rationale for the fraud on the market theory. However, for purposes of bringing liability of offenders to manageable levels, it is generally recommended that Zambian legislators and policy makers introduce ‘a rebuttable presumption of reliance’ in section 167 of the Securities. This proposal is rationalized in the next subsection.

[29] Section 130 of the Ontario Securities Act
[30]Ibidem
[31] Section 131 of the Ontario Securities Act
[32]See,*Maxwell v MLG Ventures Ltd (1995)*(Unreported, Ontario Superior Court of Justice, Ground J)

Obviously, relieving injured persons of the burden of proving reliance increases the likelihood of success of their actions. An argument could be made that such a positive feature in the Zambian legal framework is likely to enhance investor protection and enhance market integrity.

Why section 167 of the Zambian Securities Act Should Introduce a Rebuttable Presumption of Reliance

The presumption of reliance that has been proposed in relation to section 167 of the Securities Act 2016 above could be rebutted by the defendant by proving that:

i) the plaintiff did not rely of the misrepresentation or would have traded anyway; or

ii) did exchange securities for any other reason; or

iii) indeed that there had only been an insignificant or inconsequential movement in the price of securities since the misrepresentation was made; or

iv) only a small number of securities had been traded on the securities market since the misrepresentation.

Critics of these defences have stated that:

"[T]henon-reliance and immateriality defences reflect a misunderstanding of the foundations of the fraud on the market theory, and an adherence to traditionalassumptions of investor behaviour which is no longer justified inlight of modern research into securities markets."[33]

Further, Hiller and Ferris (1990) observe that:

“The non-reliance defence is improper economically because the question should be whether the market was affected rather than the individual. The injury is passed through the market. The non-reliance defence can produce inconsistent results in the determination of individual cases, when investors were affected by the same market fluctuations.”[34]

Although these judicial interventions—the defences to the fraud on the approach—are clearly inconsistent with the efficient market hypothesis, the legal approach to causation of loss for misleading statements takes consistent with the efficient market hypothesis. The legal approach

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[33]Note, The Fraud on the Market Theory: Efficient Markets and the Defences to an Implied 10b-5 Action, 70 IowAL.REv. 975, 978 (1985)

[34] Janine S. Hiller and Stephen P. Feriis, ‘Use of Economic Analysis in Fraud on the Market Cases,’ Cleveland State Law Review, Vol. 38:4, (1990), pp. 534-557, at p. 548

to causation only takes the analysis a little further in order to somehow place a cap on the quantum of liability that could possibly result from strict application of the economic approach to causation. It is therefore submitted that the said judicial interventions—the defences for rebutting the presumption of reliance—are designed to strike a balance between the need to make procedurally easier for the injured investor to recover their loss and the need to stem the liability of the defendant to manageable levels. As Hiller and Ferris (1990) further observe:

"The inconsistency between the economic and legal significance attached to non-reliance can be traced to different interpretations of causation. The economic viewpoint is that if the investor trades in a market that has been misled, which therefore reflects an incorrect valuation of the security, the investor has been injured. The legal approach encompasses thatreasoning, but requires additional proof of another type of causation. Some courts call the first type of causation, loss causation. It amounts to proof of economic loss. However, proof of economic loss only, without the requirement of a closer nexus, could effectively create a type of strict liability for an investor's injury. To avoid this, courts have also requiredproof of transaction causation. This means that there must be a link, more than damages, between the defendant and plaintiff. This link is the reliance on the market. If the plaintiff exchanged securities for anotherreason or would have traded anyway, then the chain of causation is broken, and the plaintiff could not recover. The purpose of transaction causation is to limit liability to manageable proportions. However, as the dissent in Basic complains, proof of non-reliance will be very difficult. A statementby the plaintiff that he relied on the integrity of the market to reflect its true value would be very difficult, if not impossible, to disprove because of its subjectivity."[35]

[35] Hiller and Ferris, ibidem

2.1.1.1.2.3.FRAUD ON THE MARKET APPROACH AND PRESUMED RELIANCE IN THE UNITED STATES

The cradle of the fraud on the market approach in the United States appears to beBlackie v Barrack.[36] In that case, a Ninth Circuitpanel granted class certification to investors who suffered loss, on purchase of a company's stock, between the release of allegedly misleading financial statements and corrective disclosure of the company's actual condition a couple of years later. The court found that 'causation as to each class member is adequately established <u>in the impersonal stock exchange context</u> by proof of purchase and of the materiality of the misrepresentations.'[37]The rationale for this stance was that material misrepresentations influence enough trading to affect the security's market price. This was in effect the birth of the 'fraud on the market' approach.[38]

In relation to misrepresentations in other disclosure documents—other than prospectuses—filed with the Securities and Exchange Commission, the court in Arthur Young & Co v United States District Court,[39] a registration statement filed with the Securities and ExchangeCommission contained a misleading statement, Lucas J, relying on the need for integrity of the regulatory process, stated:

"Just as the open market purchaser relies on the integrity of the market and
the price of the security traded on the open market to reflect the true value of
the securities in which he invests, so the purchaser of an original issue of a
securityrelies, at least indirectly, on the integrity of the regulatory process and
the truth of any representations made to the appropriate agencies and the
investors at the time of the original issue."[40]

Rebutting the Presumption of Reliance under the Fraud on the Market Approach

[36] 524 F 2d 891 (9th Cir, 1975), certificate denied 429 US 816 (1976)
[37] Blackie vs Barrack, per koelsch J, at p. 906
[38]This decision also appeared to extend presumed reliance beyond the earlier cases of omissions to cases of positivelyuntrue statements. It could be argued that the latter could not have occurred without the utilisation of the 'fraud on the market' approach, which provided a form of causation whereby a material misrepresentation fed into the market priceis presumed to impact anyone who purchased a security.

[39]549 F 2d 686 (9th Cir, 1977)
[40]Ibidem

In Blackie v Barrack, the court stated that the presumption of reliance was in fact rebuttable. Thus, it was open to the defendant to rebut the ‘fraud on the market’ ‘presumption of reliance’. This could be achieved in two ways, namely:

i) by proving that an insufficient number of securities was actually traded in reliance on the misrepresentation to have actually inflated the price;[41]

ii) by showing, in relation to individual plaintiffs, that they proceeded to make purchases despite knowledge of the falsity of the representation or that the person would have purchased in any event, even if he or she had known about the misrepresentation.[42]

BASIC INC vs LEVINSON

Although the fraud on the market approach in the United States was enunciated by lower courts, in due course the Supreme Court had occasion to endorse it and further put it in proper perspective. Thus, approval of the fraud on the market approach was given by the United States Supreme Court in Basic Inc. vs Levinson.[43]The facts of this case were as follows: Corporate officers of the defendant—Basic Inc.—made three public denials,two years running (between 1977 and 1978),of the existence of on-going merger negotiations with Combustion Industrial Inc. In fact the merger negotiations had been on since October 1976. The plaintiffs sold off their share in Basic Inc. after Basic Inc.’s first denial. Later, in December, 1978, Basic Inc.announced that it would merge with Combustion Industrial. This announcement resulted in a sudden sharp rise in share price of Basic Inc.’s shares. The plaintiffs alleged a violation of r 10b-5 of theSecurities Exchange Act of1934, and arguedthat the public denials of existence of merger negotiations were misleading and as such had artificially depressed the stock price thereby causing loss to the plaintiffs when they sold off their shares. In defence, the defendant alleged that no premature disclosure of merger negotiations was mandated under the rule and that such information only became material, when an agreement—in principle—had actually been reached.

Restating the significance of the requirement of materiality, the Supreme Court held thatdisclosure was mandated when the information became material for a reasonable investor’s

[41] Blackie vs Barrack, per Koelsch J, at 906
[42]Ibidem
[43]485 US 224, (1988)

decision.[44] The Court held that on-going merger negotiations were not material for a reasonable investor's decisions. The Court stated:

"The application of this materiality standard to preliminary merger discussions is not self-evident. Where the impact of the corporate development on the target's fortune is certain and clear, the TSC Industries[45]materiality test admits of straight-forward application. Where, on the other hand, the event is contingent or speculative in nature, it is difficult to ascertain whether the 'reasonable investor' wouldhaveconsidered the omitted information significant at the time.

Mergernegotiations, because of the ever-present possibility that the contemplated transaction will not be effectuated, fall into the latter category."[46]

Having resolved the issue of 'materiality', on the question of reliance and validity of the fraud on the market theory, the Court stated:

"The fraud on the market theory is based on the hypothesis that, in an open and developed securities market, the price of a company's stock isdetermined by the available material information regarding the company and its business. …Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements. … The causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations. Our task, of course, is not to assess the general validity of the theory, but to consider whether it was proper for the courts below to apply a rebuttable presumption of reliance, supported in part by the fraud-on-the-market theory."[47]

[44]*Basic Inc. vs Levinson, at 231-2*. Thus, under the Zambian legal framework, a statement is material for a reasonable investor's decision 'if and only if it affects or could reasonably be expected to affect the price or value of securities of the issuer': see, definition of 'misrepresentation' and 'material fact' in section 2 of the Zambian Securities Act 2016

[45]*TSC Industries Inc. vs Norway Inc,* 426 US 438 (1976). In *TSC Industries Inc.*, it was earlier held that a matter 'is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. Per Justice Marshall

[46] Basic Inc. vs Levinson, at 232

While noting that proof of individual reliance was traditionally a necessary prerequisite to success of common law fraud claims, the Court nonetheless affirmed the application of the fraud on the market theory in favour of investors and the rebuttability of the presumptionin favourof defendants:

"…[M]odern securities markets, literally involving millions of shares changinghands daily, differ from the face-to-face transactions contemplated by early fraud cases, and our understanding of r 10b-5's reliance requirement must encompass these differences. … Requiring a plaintiff to show a speculative state of facts, that is, how he would have acted if omitted materialinformation had been disclosed, or if the misrepresentation had not been made, would place an unnecessarily unrealistic evidentiary burden on the Rule 10b-5 plaintiff who has traded on an impersonal market. Arising out of considerations of fairness, public policy, and probability, as well as judicial economy, presumptions are also useful devices for allocating theburdens of proof between the parties. The presumption of reliance employed in this case is consistent with, and, by facilitating Rule 10b-5 litigation, supports, the congressional policy embodied in the 1934 Act. The presumption is also supported by common sense and probability. Recent empirical studies have tended to confirm Congress' premise that the marketprice of shares traded on well-developed markets reflects all publicly availableinformation, and, hence, any material misrepresentations. It has been noted that 'it is hard to imagine that there ever is a buyer or seller who does not rely on market integrity. Who would knowingly roll the dice in a crooked crap game?'… Because most publicly available information is reflected in market price, an investor's reliance on any public material misrepresentations, therefore, may be presumed for purposes of a Rule 10b-5 action."[48]

[47]Ibid 241–2
[48]Ibid 243–7

2.2.APPROACH TO CAUSATION AND LOSS FOR PURE NON-DISCLOSURE

In Peek vs Gurney[49], it was held that there is no general duty of disclosure. Thus, without a duty to disclose, there is no liability for failure or neglect to disclose. Mandatory disclosure consists in either periodic or continuous disclosure.[50]

Continuous disclosure can be defined as an obligation to promptly disclose material new non-public information concerning a listed issuer as and when it becomes known to the officers of the issuer. This obligation may be contrasted, in the Zambian context, with periodic disclosure which requires preparation and filing of annual disclosure documents.[51] In distinguishing continuous disclosure from periodic disclosure, Golding and Kalfus (2004) observe:

> "[A] key distinction between periodic disclosure and continuous disclosure
> is that periodic disclosure is episodic and permits information to be refined
> and disclosure issues to be assessed over an appropriate period following
> the relevant closing date of the financial statement, while continuous
> disclosure is prompt, resulting in the need to make speedy disclosure
> decisions."[52]

2.2.1.THE RIGHT TO CIVIL RECOVERY FOR LOSS CAUSED BY PURE NON-DISCLOSURE

Under the Zambian legal framework for the public distribution of securities, there is no right to civil recovery of loss occasioned by pure non-disclosure not resulting in misrepresentation.[53] However, where pure non-disclosure results in misrepresentation—as in where a registered disclosure document is rendered misleading when viewed in light of the undisclosed

[49](1873) LR 6 HL 377

[50] There is also an implied duty to disclose as in cases where an insider, a tipee or information abuser acquires or disposes securities. In such a case, they have an implied duty to disclose to the other party to the contract the inside information or altogether refrain from dealing in securities.

[51] See, section 185 of the Companies Act 1994 which imposes an obligation on public companies to make annual returns. A public company is under an obligation to lodge with the Registrar such return within one month after the Annual General Meeting, and if the AGM is held within three months after the end of the financial year, within three months from the end of the financial year: Section 184(1)(a)(b) of the Companies Act 1994.

[52] Greg Golding and NatalleKalfus, 'The Continuous Evolution of Australia's Continuous Disclosure Laws,' Company & Securities Law Journal, Vol. 22 of 2004, p. 385, at pp. 385-386

[53] See, Samamba, Lennox Trivedi, 'The Zambian Continuous Disclosure Legal Regime—Adequate to Ensure Efficient Disclosure?,' Law Association of Zambia Law Journal, Vol. 5, 2018

information—the injured person may have recourse to the recovery procedure provided under Part XV of the Zambian Securities Act 2016.

2.2.2. APPROACH TO CAUSATION AND LOSS FOR PURE NON-DISCLOSURE

If the misrepresentation resulting from the pure non-disclosure relates to a prospectus, the recovery procedure provided under section 166 of the Securities Act 2016 would apply; this would imply that the common law approach to causation and loss for misrepresentation provided therein applies. In the event that the resultant misrepresentation relates to other disclosure documents than prospectuses, the recovery procedure available under section 167 of the Securities Act 2016 applies; in such a case, the fraud on the market approach to causation and loss for misrepresentation and non-disclosure—in its purest form—would apply. Quite clearly, there exists two distinct approaches to civil recovery for loss caused by pure non-disclosure amounting to misrepresentation as there are for loss occasioned by pure misrepresentation under Part XV of the Securities Act 2016.

2.2.3.APPROACH TO CAUSATION AND LOSS FOR PURE NON-DISCLOSURE IN AUSTRALIA

It is worth-noting that the American judicial approach to causation and loss for non-disclosure (half-truths) earlier discussed were discussed in the context of misrepresentation resulting from such non-disclosure and not pure non-disclosure resulting from breach of the continuous disclosure obligation. The contrary could not be and cannot be on account of absence of the continuous disclosure obligation under the United States securities laws.

Continuous DisclosureObligation under the United States Federal Securities Laws?

Case law dealing with the continuous duty to update already disclosed information by issuer in the United States is inconsistent on the issue. In Backman v. Polaroid Corp.[54], the First Circuit Court has unequivocally held that a duty to update exists in the United States under federal laws, stating that:

[54]Backman v. Polaroid Corp., 910 F.2d 10 (1st Cir. 1990)

"[w]e may agree that, in special circumstances, a statement, correct at the time, may have a forward intent and connotation upon which parties may be expected to rely. If this is a clear meaning, and there is a change, correction, more exactly, further disclosure, may be called for."[55]

However, the more recent decisions of Stransky v. Cummins Engine Co., Inc[56]., Eisenstadt v. CentelCorp[57]., and Gallagher v. Abbott Labs.[58],all decided by the Seventh Circuit Court, cast some doubt on the recognizing a duty to update—continuous disclosure obligation. The Seventh Circuit Court in Gallagher held that:

"[T]here is no continuous duty to update on the part of the issuer…..federal securities laws do not require continuous disclosure but rather, only require issuers to file periodic reports."[59]

Be as it may, where the court holds that the duty to update—continuously disclose information so as to correct the false impression made by the already disclosed information—exists, a persons who sells or purchases securities at an under-value or over-value may commence statutory civil class actions against the issuer under federal laws.

III

3.MAKING A CASE FOR ADOPTION OF THE FRAUD ON THE MARKE THEORY AS THE SOLE APPROACH TO CAUSATION OF LOSS FOR MISREPRESENTATION AND NON-DISCLOSURE

The case for adopting the fraud on the market theory as the sole approach to causation and loss for misrepresentation in disclosure documents and pure non-disclosure seems to consist in the following, namely:

i) regulatory efficacy of the basis for the fraud on the market theory;

ii) limitations inherent in the common law based reliance approach;

iii) thesmall size of the Zambian securities market.

[55]Ibidem, p. 17

[56]Stransky v. Cummins Engine Co., Inc., 51 F.3d 1329, 1332 (7th Cir. 1995)

[57]Eisenstadt v. Centel Corp., 133 F.3d 738, 746 (7th Cir. 1997)

[58] Gallagher v. Abbott Labs., 269 F.3d 806, 809 (7th Cir. 2001)

[59]Ibidem, at p. 810

3.1.REGULATORY BASIS FOR THE FRAUD ON THE MARKET APPROACH

The regulatory basis for the fraud on the market theory consists in two significant influences on securities law—the efficient capital market hypothesis, investor class actions and SEC's representative actions.

3.1.1.THE EFFICIENT CAPITAL MARKETS HYPOTHESIS

The theoretical underpinning of fraud on the market theory is the efficient capital market hypothesis.[60]An efficient securities market is one that rapidly reflects new information in a security's price without bias;[61] that is, the more rapidly the market incorporates new information into a security'sprice, the more efficient the market.[62] In a fully efficient market, an investor cannot achieve a return on his investment that is greater than the market average through securities research.[63]

The relaxed version of the efficient capital market hypothesis holds that the price of a particular security in the securities market quickly reflects all relevant, publicly available information.[64] The relaxed version of the hypothesis provides a theoretically coherent and empirically tested mechanism to substantiate the central premise of the fraud on the market theory.[65]Thus, when a material misrepresentation enters the stream of publicly available information, it is quickly incorporated into the security's market price, thereby artificially inflating or, less often so, deflating the price.[66] Similarly, non–disclosure of informationcrates an informational void or bubble in the stream of publicly available information thereby artificially inflating or deflating the price of security. Consequently, because the market incorporates all publicly available information into a security's price, investors should be able to reasonably rely on the efficiency of the market to price securities accurately.[67]Thus, the hypothesis seems to validate the fraud on

[60]See,Daniel R. Fischel, 'Efficient Capital Markets, the Crash, and the Fraud on the Market Theory', 74 Cornell L. Rev. 907, 910-12 (1989)
[61]Ibidem
[62]Ibidem
[63] Daniel R. Fischel, 'Efficient Capital Market Theory, the Market for Corporate Control, and the Regulation of Cash Tender Offers,'57 Tex. L. Rev. 1, 3-4 (1978)
[64]Danniel R. Fischel (1989), at p. 911, *op.cit*
[65]See, Basic Inc. v. Levinson, 485 U.S. 224, at p.246
[66]Ibidem
[67]Ibidem

the marketapproach—that the defendant's misrepresentation caused the plaintiff's injury even though plaintiff did not actually/directly rely on the defendant’s misrepresentations.[68] Also, in the case of pure non-disclosure, the defendant’s non-disclosure should be taken to be the cause of the loss of the plaintiff even if the plaintiff did not in fact rely on the undisclosed facts.

Other Policy Justifications for the Fraud on the Market Approach

Another argument for the fraud on the market consists in the need to enhance market integrity by deterring all forms of securities market misconduct. An argument is made here that just as the criminal law relating to inchoate offences—such as attempts—is designed to enhance societal order by looking at the state of mind of the accused as opposed the impact of the act or omission of the accused, even so should the fraud on the market theory be employed as a device for enhancing order on securities markets by looking to the conduct of the offender and its effect on the market as opposed to looking at its direct influence on the investment decision of the injured person. Looking to the conduct of a market participants and its impact on the integrity of the securities market rather than on reliance is likely to deter market misconduct that has the potential of hurting the integrity of the market and eroding investor confidence. This argument is further fortified by the following scenario: XCo files disclosure documents with the SEC and makes the same available to LuSE. In fact these disclosure documents are full of serious misstatement relating to the profitability and growth potential of the company. Twenty four hour later, the price of XCo securities rises by 65 per cent. Y, without the knowledge of these misleading statements, buys quite a number of these XCo securities at K10 per share. Six months later, Z—the chief executive officer of XCo—makes corrective statement by stating the true position as it stood six months ago when Y bought the securities. As a consequence of the corrective announcement, the price of XCo securities plummeted by 90 per cent. The common law approach, would deny Y success in her action of misrepresentation since she did not rely on misstatements made by XCo. Would not such a shortcoming in the law discourage Y and other similarly circumstanced investors from further participation in the securities market? Would not such a negative feature in the law—the reliance approach—hurt the integrity of the securities market and erode investor confidence? We think the answers to the above questions are in the affirmative.

[68]Ibidem

3.1.2.INVESTOR CLASS ACTIONS AND SEC'S REPRESENTATIVE ACTIONS

The Zambian legal framework does not provide for investor class action whereby on injured investor is allowed to commence and maintain a civil recovery action on his or behalf and on behalf of similarly circumstanced investors. What the Zambian legal framework provides is SEC's representative civil actions. The power on the part of the Zambian SEC to commence representative civil action for and on behalf of injured investors and issuers—who for some reason or the other are unable to commence such actions—is designed to preserve the integrity of the Zambian securities market. The integrity of the Zambian securities market consists, in part, in the fairness, efficiency, financial integrity of transactions and safeguards against systemic risk in securities markets.[69] In this context, introduction of the fraud on the market approach to causation and loss for misrepresentation and pure non-disclosure could be said to be an invaluable additional arsenal to SEC's armoury for preserving securities market integrity and enhancing investor confidence through effective enforcement of regulatory rules.

3.2.LIMITATIONS INHERENT IN THE COMMON LAW BASED RELIANCE APPROACH

Let us assume that the Y's loss in the scenario above is caused by XCo's partial disclosure made in a prospectus or XCo's failure or neglect to make continuous disclosure which rendered already disclosed facts in the registered prospectus misleading. Let us also assume that Y's loss was caused by revelation of purely undisclosed material facts by XCo. Quite obviously, Y's civil recovery action of misrepresentation consisting in half-truths or partial disclosure or a civil recovery action for non-disclosure is bound to fail on account of lack of reliance. How could Y possibly rely on undisclosed facts?

As a possible solution to this shortcoming in the law proposals are made for the introduction of the fraud on the market approach into section 166 of the Zambian Securities Act 2016 as a means of lessening evidentiary and procedural burdens cast on injured investors by the reliance approach in their quest for damages for loss occasioned by misrepresentation in disclosure documents or pure non-disclosure. In the case of pure non-disclosure consisting in breach of the

[69] See, the Long Title to the Zambian Securities Act 2016

continuous disclosure obligation, it is hoped that the Capital Markets Tribunal will adopt the fraud market approach to causation and loss caused by pure non-disclosure as a vessel for navigating around the evidentiary and procedural hurdles caused by the common law reliance approach which has its origin in fraud cases—deceit or fraudulent misrepresentation.

3.3.THE SMALL SIZE OF THE ZAMBIAN SECURITIES MARKET

Misrepresentation pluming into the information stream on a securities market or informational bubbles or void created by pure non-disclosure may not have the same adverse impact on a small and shallow market as it would a larger developed and deeper market. Along these lines, given the nascent stage in the development of the Zambian securities market, the adoption of the fraud on the market as regulatory device for deterring securities misconduct is justified.

3.4.EXTENSION OF THE FRAUD ON THE MARKET APPROACH TO PRIMARY AND FRESH ISSUES OF SECURITIES IN THE UNITED STATES

In Arthur Young & Co. v. United States District Court[70], the defendant had sold limited partnership interests in oil andgas exploration ventures to members of the plaintiff class pursuant to anallegedly misleading registration statement filed with the SEC.The Ninth Circuit found that misrepresentations and non-disclosures in disclosure materials in an undeveloped primary market merited a similar presumption of reliance that the court had earlier granted to the plaintiffs in Blackie v. Barrack in a developed market scenario two years earlier.

Four years later, the Fifth Circuit in Shores vsSklar71, extended the presumption of reliance, for the first time, to a primary market involving a fresh issue of securities consisting in revenue bonds. Thus, the plaintiff stated a claim under Rule 10b-5(a) and (c)'sgeneralized anti-fraud language. Seeing that there was no reliance on the misrepresentations in the offering circular, the Fifth Circuit formulated a standard for extending the presumption of reliance to the plaintiffs in the primary market context. The Court held that investors could rely on the market to preclude

[70] 549 F.2d 686 (9th Cir.), *cert. denied*, 434 U.S. 829 (1977).
[71] 647 F.2d 462 (5th Cir. 1981), *cert. denied*, 459 U.S. 1102 (1983).

securities that, but for defendants' fraud, were not 'entitled to be marketed'.[72]In order to recover their loss, plaintiff must show the following:[73]

i) the defendants knowingly conspired to bring securities onto the market which were not entitled to be marketed, intending to defraud purchasers;

ii) plaintiff reasonably relied on the bonds' availability on the market as an indication of their apparent genuineness; and

iii) as a result of the scheme to defraud, plaintiff suffered a loss.

Thus, where the plaintiff(s) allege(s) a generalized scheme to defraud investors that was not limited to misstatements in the disclosure documents, lack of direct reliance on the disclosure documents would not preclude recovery by the plaintiff(s).

In the interest of enhancing market integrity and growing investor confidence, it is generally recommended that the Zambian Capital Markets Tribunal adopts this sought of approach as a device for ensuring that investors, who suffer loss as result of misrepresentations or omissions in prospectuses or pure non-disclosure of information relating to a fresh issue of securities in a primary market, are not precluded from recovering their loss by the unavoidable non-reliance in such cases.

4.CONCLUSION

The general conclusion reached in this article is that the legal framework for the public distribution of securities has not provided adequate incentives for civil recovery, by investors, of loss occasioned by misrepresentations or omissions in prospectuses, or pure non-disclosure.

In particular, the article has established that the Zambian legal framework for public distribution of securities has adopted total distinct approaches to causation and loss for misrepresentation in prospectuses and other disclosure documents. In this context, it has been established that while an investor would have to prove reliance in order to recover in respect of loss caused by misrepresentations or omissions in prospectuses, they need not do so in relation to misrepresentations or omissions in other disclosure documents. The article has further

[72]*Shores vsSklar, at p. 469*
[73]Ibidem

established that in cases of partial disclosure or pure non-disclosure, it would be practically impossible to prove reliance on undisclosed facts. In this regard, an argument has been made that such a procedural shortcoming in the law is likely to discourage participation in fresh or new issues of securities in the primary market where the prospectus in traditionally used. An argument is also made that such procedural hurdles are likely to incentivize partial or pure non-disclosures prospectuses in relation to new issues of securities, hurt the integrity of the market and dampen investor confidence.

As a possible solution to the said shortcomings in the law, proposals have been made for the adoption of the fraud on the market theory as device for easing recovery by investors by doing away with the requirement of proving reliance before a civil recovery action can succeed.