Public Law 100-704
100th Congress

An Act

To improve the procedures and remedies for the prevention of insider trading, and for other purposes.

Nov. 19, 1988
[H.R. 5133]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Insider Trading and Securities Fraud Enforcement Act of 1988.
15 USC 78a note.

SECTION 1. SHORT TITLE.

This Act may be cited as the "Insider Trading and Securities Fraud Enforcement Act of 1988".

15 USC 78u-1 note.

SEC. 2. FINDINGS.

The Congress finds that—

(1) the rules and regulations of the Securities and Exchange Commission under the Securities Exchange Act of 1934 governing trading while in possession of material, nonpublic information are, as required by such Act, necessary and appropriate in the public interest and for the protection of investors;

(2) the Commission has, within the limits of accepted administrative and judicial construction of such rules and regulations, enforced such rules and regulations vigorously, effectively, and fairly; and

(3) nonetheless, additional methods are appropriate to deter and prosecute violations of such rules and regulations.

SEC. 3. CIVIL PENALTIES OF CONTROLLING PERSONS FOR ILLEGAL INSIDER TRADING BY CONTROLLED PERSONS.

(a) AMENDMENT.—The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended—

15 USC 78u.

(1) in section 21(d)—

(A) by striking out paragraph (2); and

(B) by redesignating subsection (d)(1) as subsection (d); and

(2) by inserting after section 21 the following new section:

"CIVIL PENALTIES

15 USC 78u-1.

"SEC. 21A. (a) AUTHORITY TO IMPOSE CIVIL PENALTIES.—

"(1) JUDICIAL ACTIONS BY COMMISSION AUTHORIZED.—Whenever it shall appear to the Commission that any person has violated any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information in, or has violated any such provision by communicating such information in connection with, a transaction on or through the facilities of a national securities exchange or from or through a broker or dealer, and which is not part of a public offering by an issuer of securities other than standardized options, the Commission—

Courts, U.S.

"(A) may bring an action in a United States district court to seek, and the court shall have jurisdiction to impose, a

AUTHENTICATED U.S. GOVERNMENT INFORMATION GPO

civil penalty to be paid by the person who committed such violation; and

Courts, U.S.

"(B) may, subject to subsection (b)(1), bring an action in a United States district court to seek, and the court shall have jurisdiction to impose, a civil penalty to be paid by a person who, at the time of the violation, directly or indirectly controlled the person who committed such violation.

"(2) AMOUNT OF PENALTY FOR PERSON WHO COMMITTED VIOLATION.—The amount of the penalty which may be imposed on the person who committed such violation shall be determined by the court in light of the facts and circumstances, but shall not exceed three times the profit gained or loss avoided as a result of such unlawful purchase, sale, or communication.

"(3) AMOUNT OF PENALTY FOR CONTROLLING PERSON.—The amount of the penalty which may be imposed on any person who, at the time of the violation, directly or indirectly controlled the person who committed such violation, shall be determined by the court in light of the facts and circumstances, but shall not exceed the greater of $1,000,000, or three times the amount of the profit gained or loss avoided as a result of such controlled person's violation. If such controlled person's violation was a violation by communication, the profit gained or loss avoided as a result of the violation shall, for purposes of this paragraph only, be deemed to be limited to the profit gained or loss avoided by the person or persons to whom the controlled person directed such communication.

"(b) LIMITATIONS ON LIABILITY.—

"(1) LIABILITY OF CONTROLLING PERSONS.—No controlling person shall be subject to a penalty under subsection (a)(1)(B) unless the Commission establishes that—

"(A) such controlling person knew or recklessly disregarded the fact that such controlled person was likely to engage in the act or acts constituting the violation and failed to take appropriate steps to prevent such act or acts before they occurred; or

"(B) such controlling person knowingly or recklessly failed to establish, maintain, or enforce any policy or procedure required under section 15(f) of this title or section 204A of the Investment Advisers Act of 1940 and such failure substantially contributed to or permitted the occurrence of the act or acts constituting the violation.

"(2) ADDITIONAL RESTRICTIONS ON LIABILITY.—No person shall be subject to a penalty under subsection (a) solely by reason of employing another person who is subject to a penalty under such subsection, unless such employing person is liable as a controlling person under paragraph (1) of this subsection. Section 20(a) of this title shall not apply to actions under subsection (a) of this section.

"(c) AUTHORITY OF COMMISSION.—The Commission, by such rules, regulations, and orders as it considers necessary or appropriate in the public interest or for the protection of investors, may exempt, in whole or in part, either unconditionally or upon specific terms and conditions, any person or transaction or class of persons or transactions from this section.

"(d) PROCEDURES FOR COLLECTION.—

"(1) PAYMENT OF PENALTY TO TREASURY.—A penalty imposed under this section shall (subject to subsection (e)) be payable into the Treasury of the United States.

"(2) COLLECTION OF PENALTIES.—If a person upon whom such a penalty is imposed shall fail to pay such penalty within the time prescribed in the court's order, the Commission may refer the matter to the Attorney General who shall recover such penalty by action in the appropriate United States district court.

"(3) REMEDY NOT EXCLUSIVE.—The actions authorized by this section may be brought in addition to any other actions that the Commission or the Attorney General are entitled to bring.

"(4) JURISDICTION AND VENUE.—For purposes of section 27 of this title, actions under this section shall be actions to enforce a liability or a duty created by this title.

"(5) STATUTE OF LIMITATIONS.—No action may be brought under this section more than 5 years after the date of the purchase or sale. This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this title, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties, imposed in an action commenced within 5 years of such transaction.

"(e) AUTHORITY TO AWARD BOUNTIES TO INFORMANTS.—Notwithstanding the provisions of subsection (d)(1), there shall be paid from amounts imposed as a penalty under this section and recovered by the Commission or the Attorney General, such sums, not to exceed 10 percent of such amounts, as the Commission deems appropriate, to the person or persons who provide information leading to the imposition of such penalty. Any determinations under this subsection, including whether, to whom, or in what amount to make payments, shall be in the sole discretion of the Commission, except that no such payment shall be made to any member, officer, or employee of any appropriate regulatory agency, the Department of Justice, or a self-regulatory organization. Any such determination shall be final and not subject to judicial review.

"(f) DEFINITION.—For purposes of this section, 'profit gained' or 'loss avoided' is the difference between the purchase or sale price of the security and the value of that security as measured by the trading price of the security a reasonable period after public dissemination of the nonpublic information.".

(b) AMENDMENTS CONCERNING SUPERVISION.—

(1) BROKERS AND DEALERS.—Section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 78o) is amended by adding at the end thereof the following new subsection:

"(f) Every registered broker or dealer shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such broker's or dealer's business, to prevent the misuse in violation of this title, or the rules or regulations thereunder, of material, nonpublic information by such broker or dealer or any person associated with such broker or dealer. The Commission, as it deems necessary or appropriate in the public interest or for the protection of investors, shall adopt rules or regulations to require specific policies or procedures reasonably designed to prevent misuse in violation of this title (or the rules or regulations thereunder) of material, nonpublic information.".

Classified information.

(2) INVESTMENT ADVISERS.—The Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) is amended by adding after section 204 the following new section:

"PREVENTION OF MISUSE OF NONPUBLIC INFORMATION

15 USC 80b-4a.

"SEC. 204A. Every investment adviser subject to section 204 of this title shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such investment adviser's business, to prevent the misuse in violation of this Act or the Securities Exchange Act of 1934, or the rules or regulations thereunder, of material, nonpublic information by such investment adviser or any person associated with such investment adviser. The Commission, as it deems necessary or appropriate in the public interest or for the protection of investors, shall adopt rules or regulations to require specific policies or procedures reasonably designed to prevent misuse in violation of this Act or the Securities Exchange Act of 1934 (or the rules or regulations thereunder) of material, nonpublic information.".

15 USC 78u-1 note.

(c) COMMISSION RECOMMENDATIONS FOR ADDITIONAL CIVIL PENALTY AUTHORITY REQUIRED.—The Securities and Exchange Commission shall, within 60 days after the date of enactment of this Act, submit to each House of the Congress any recommendations the Commission considers appropriate with respect to the extension of the Commission's authority to seek civil penalties or impose administrative fines for violations other than those described in section 21A of the Securities Exchange Act of 1934 (as added by this section).

SEC. 4. INCREASES IN CRIMINAL PENALTIES.

Section 32(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78ff(a)) is amended—

(1) by striking "$100,000" and inserting "$1,000,000";

(2) by striking "five years" and inserting "10 years";

(3) by striking "is an exchange" and inserting "is a person other than a natural person"; and

(4) by striking out "$500,000" and inserting "$2,500,000".

SEC. 5. LIABILITY TO CONTEMPORANEOUS TRADERS FOR INSIDER TRADING.

The Securities Exchange Act of 1934 is amended by inserting after section 20 the following new section:

"LIABILITY TO CONTEMPORANEOUS TRADERS FOR INSIDER TRADING

Classified information. 15 USC 78t-1.

"SEC. 20A. (a) PRIVATE RIGHTS OF ACTION BASED ON CONTEMPORANEOUS TRADING.—Any person who violates any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

"(b) LIMITATIONS ON LIABILITY.—

"(1) CONTEMPORANEOUS TRADING ACTIONS LIMITED TO PROFIT GAINED OR LOSS AVOIDED.—The total amount of damages imposed under subsection (a) shall not exceed the profit gained or

loss avoided in the transaction or transactions that are the subject of the violation.

"(2) OFFSETTING DISGORGEMENTS AGAINST LIABILITY.—The total amount of damages imposed against any person under subsection (a) shall be diminished by the amounts, if any, that such person may be required to disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 21(d) of this title relating to the same transaction or transactions.

"(3) CONTROLLING PERSON LIABILITY.—No person shall be liable under this section solely by reason of employing another person who is liable under this section, but the liability of a controlling person under this section shall be subject to section 20(a) of this title.

"(4) STATUTE OF LIMITATIONS.—No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

Classified information.

"(c) JOINT AND SEVERAL LIABILITY FOR COMMUNICATING.—Any person who violates any provision of this title or the rules or regulations thereunder by communicating material, nonpublic information shall be jointly and severally liable under subsection (a) with, and to the same extent as, any person or persons liable under subsection (a) to whom the communication was directed.

"(d) AUTHORITY NOT TO RESTRICT OTHER EXPRESS OR IMPLIED RIGHTS OF ACTION.—Nothing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this title or the availability of any cause of action implied from a provision of this title.

"(e) PROVISIONS NOT TO AFFECT PUBLIC PROSECUTIONS.—This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this title, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties.".

SEC. 6. INVESTIGATORY ASSISTANCE TO FOREIGN SECURITIES AUTHORITIES.

(a) DEFINITION OF FOREIGN SECURITIES AUTHORITY.—Section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)) is amended by adding at the end thereof the following:

"(50) The term 'foreign securities authority' means any foreign government, or any governmental body or regulatory organization empowered by a foreign government to administer or enforce its laws as they relate to securities matters.".

(b) AUTHORITY TO PROVIDE ASSISTANCE TO FOREIGN SECURITIES AUTHORITIES.—Section 21(a) of such Act (15 U.S.C. 78u(a)) is amended—

(1) by redesignating subsection (a) as subsection (a)(1); and

(2) by adding at the end thereof the following:

"(2) On request from a foreign securities authority, the Commission may provide assistance in accordance with this paragraph if the requesting authority states that the requesting authority is conducting an investigation which it deems necessary to determine whether any person has violated, is violating, or is about to violate any laws or rules relating to securities matters that the requesting authority administers or enforces. The Commission may, in its discretion, conduct such investigation as the Commission deems necessary to

collect information and evidence pertinent to the request for assistance. Such assistance may be provided without regard to whether the facts stated in the request would also constitute a violation of the laws of the United States. In deciding whether to provide such assistance, the Commission shall consider whether (A) the requesting authority has agreed to provide reciprocal assistance in securities matters to the Commission; and (B) compliance with the request would prejudice the public interest of the United States.".

15 USC 78b note.

SEC. 7. SECURITIES LAWS STUDY.

(a) FINDINGS.—The Congress finds that—

(1) recent disclosures of securities fraud and insider trading have caused public concern about the adequacy of Federal securities laws, rules, and regulations;

(2) Federal securities laws, rules, and regulations have not undergone a comprehensive and exhaustive review since the advent of the modern international, institutionalized securities market;

(3) since that review, the volume of securities transactions and the nature of the securities industry have changed dramatically; and

(4) there is an important national interest in maintaining fair and orderly securities trading, assuring the fairness of securities transactions and markets and protecting investors.

(b) STUDY AND INVESTIGATION REQUIRED.—

(1) GENERAL REQUIREMENT.—The Securities and Exchange Commission shall, subject to the availability of funds appropriated pursuant to subsection (d), make a study and investigation of the adequacy of the Federal securities laws and rules and regulations thereunder for the protection of the public interest and the interests of investors.

(2) REQUIRED SUBJECTS FOR STUDY AND INVESTIGATION.—Such study and investigation shall include an analysis of—

(A) the extent of improper trading while in possession of insider information, such as trading with advance knowledge of tender offers or forthcoming announcements of material financial information;

(B) the adequacy of surveillance methods and technologies of brokers, dealers, and self-regulatory organizations;

(C) the adequacy of cooperation between the Federal, State, and foreign enforcement authorities concerning securities laws enforcement; and

(D) impediments to the fairness and orderliness of the securities markets and to improvements in the breadth and depth of the capital available to the securities markets, and additional methods to promote those objectives.

(3) CONDUCT OF STUDY AND INVESTIGATION.—In conducting the study and investigation required by this section, the Commission—

(A) may exercise any existing authority to gather information, including all power and authority the Commission would have if such investigation were being conducted pursuant to section 21 of the Securities Exchange Act of 1934;

(B) may consult with and obtain such assistance and information from other agencies in the executive and legis-

lative branches of the Government (including the Department of Justice) as is necessary to enable the Commission to carry out this section;

(C) may appoint, without regard to the civil service laws, rules, and regulations, such personnel as the Commission deems advisable to carry out such study and investigation and to fix their respective rates of compensation without regard to such laws, rules, and regulations, but no such rate shall exceed the rate payable pursuant to section 5314 of title 5, United States Code; and

(D) may, on a reimbursable basis, use the services of personnel detailed to the Commission from any Federal agency.

(4) SUPPORT FROM OTHER AGENCIES.—(A) The head of any Federal agency—

(i) may detail employees to the Commission for the purposes of this section; and

(ii) shall provide to the Commission such information as it requires for the performance of its functions under this section, consistent with applicable law.

(B) The Comptroller General and the Director of the Office of Technology Assessment are authorized to assist the Commission in the performance of its functions under this section.

(c) REPORTS AND INFORMATION TO CONGRESS.—

(1) GENERAL REPORT.—The Commission shall report to the Congress on the results of its study and investigation within 18 months after the date funds to carry out this section are appropriated under subsection (d). Such report shall include the Commission's recommendations, including such recommendations for legislation as the Commission deems advisable.

(2) INTERIM INFORMATION TO CONGRESS.—The Commission shall keep the Committee on Energy and Commerce of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate, and the members thereof, fully informed on the progress of, and any impediments to completing, the study and investigation required by this section.

(d) AUTHORIZATION OF APPROPRIATIONS.—There are authorized to be appropriated $5,000,000 to carry out the study and investigation required by this section.

(e) DEFINITIONS.—As used in this section—

(1) the term "Commission" means the Securities and Exchange Commission; and

(2) the term "Federal securities laws" has the meaning given the term securities laws by section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)).

SEC. 8. COOPERATION WITH FOREIGN AUTHORITIES AND INTERNATIONAL ORGANIZATIONS IN ENFORCEMENT.

Section 35 of the Securities Exchange Act of 1934 is amended by adding at the end thereof the following new subsection: 15 USC 78kk.

"(c) Funds appropriated pursuant to this section are authorized to be expended—

"(1) for official reception and representation expenses, not to exceed $10,000 per year; and

"(2) for the purpose of maintaining membership in and contributing to the operating expenses of the International

Organization of Securities Commissions, not to exceed $10,000 per year.".

15 USC 78*o* note.

SEC. 9. EFFECTIVE DATE.

The amendments made by this Act, except for section 6, shall not apply to any actions occurring before the date of enactment of this Act.

Approved November 19, 1988.

LEGISLATIVE HISTORY—H.R. 5133:

HOUSE REPORTS: No. 100-910 (Comm. on Energy and Commerce).
CONGRESSIONAL RECORD, Vol. 134 (1988):
Sept. 13, 14, considered and passed House.
Oct. 21, considered and passed Senate.