

ARTICLE

Congressional Insider Trading Is Already Illegal

Roll Call

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"Insider Trading Laws Don't Apply to Congress!" It's no surprise that headlines such as this one outrage the public. But it's not true.

Current insider trading prohibitions do apply to Members of Congress and staffers. If the Stop Trading on Congressional Knowledge Act is enacted, it would impose restrictions on securities trading by Senators, Representatives and Congressional staff beyond those to which they are already subject under federal law — and, arguably, beyond those that apply to the American public generally.

Many may think this would be a good outcome. But if it's not the outcome Congress intends, the STOCK Act, at least in its current form, needs to be considered very carefully.

Just like the rest of us, a Member or employee of Congress who trades stocks could be prosecuted under the "misappropriation" theory of insider trading — upheld by the Supreme Court in its 1997 *U.S. v. O'Hagan* decision — if he or she trades on the basis of material, nonpublic information obtained from a source to which he or she owes a duty of confidentiality.

In his recent testimony on the bill before the House Financial Services Committee, Robert Khuzami, director of the Securities and Exchange Commission's Division of Enforcement, confirmed that Members and staff are not exempt from insider trading prohibitions.

The securities laws and rules themselves, then, do not interpose any legal stumbling blocks to bringing a Congressional insider trading case. On the other hand, it could be very difficult in the

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Congressional context to find factual proof sufficient to support an insider trading allegation (even leaving aside unique issues that could be posed by Members' privilege under the Speech or Debate Clause of the Constitution).

One important question in any Congressional insider trading case would be: Was the Congressional information on the basis of which a transaction in a company's securities was made really material — that is, would a reasonable shareholder consider that information important in making an investment decision?

Particularly where, as is so often the case, Congressional action on a matter comes well after disclosures in other arenas about a company, information about such things as the scheduling of hearings or even about proposed legislation is likely to be seen as moot — rather than as material — by most investors.

Another hurdle: Given the swirl of information sweeping through the Capitol — and the microscopic and perpetual coverage of Congressional business in the age of new media — can the specific information traded on really be considered nonpublic? And did the Member or staffer have an actual duty to keep the information confidential?

When is Congressional information confidential? Some committees — the Ethics and Intelligence panels, for example — by rule impose obligations of confidentiality or secrecy on Members and staff. Proceedings of the House and Senate in closed session may be subject to an "injunction of secrecy." But there is no blanket designation of all information coming before Congress as "confidential." Should there be?

The STOCK Act, in effect, answers "yes," at least when the information is used in connection with a securities trade. Under the bill, a Member or employee who trades in securities based on material, nonpublic information will be deemed to have engaged in insider trading if that information "was obtained by reason of such person being a Member or employee of Congress," regardless of whether any other specific duty of confidentiality may be deemed to exist.

Some argue that this approach is too broad, that it will not only deter improper "insider" trading but could well deter most other, perfectly legitimate, buying and selling of securities by Members and staff, or force them to put their assets in cumbersome blind trusts. To which others may, in reply, offer a resounding chorus of: "So what? If people want to serve the public they should be willing to sacrifice private financial interest." Yes they should, but to what degree? With super-strictures on their financial decision-making such as those that may be imposed by the STOCK Act, will government service attract the best and the brightest, or even the pretty good and the fairly smart?

Beyond potentially imposing additional insider trading restrictions on Members and staffers, the STOCK Act would subject any person to prosecution for insider trading if done on the basis of material, nonpublic information obtained from a Member or employee of Congress.

It is not hard to imagine the profound chilling effect this could have on the legitimate exchange of information and ideas by Members and staff with individuals of all kinds outside Congress.

Building a more accountable Congress is a goal with which everyone should agree. But, because it is based on a mistaken legal premise, is the STOCK Act the best way to reach that goal?