

The SEC Latest Effort to Combat Insider Trading

By Natasha Meruelo, The Nelson Law Firm, LLC

Originally Published in *Traders Magazine* on September 2, 2008

<http://www.tradersmagazine.com/news/101941-1.html>

In the past few years, the Securities and Exchange Commission has focused much of its enforcement energies on combating insider trading. The result has been significant victories for the SEC against insider traders and the imposition of large fines on several hedge fund portfolio managers, among others. Despite the increased enforcement, insider trading continues to occur in the trading community at large, with no end in sight. Since February 2007, the SEC has brought eighteen enforcement actions against various persons, including entire families, the Mayor of Beaufort, S.C., CEOs and other business insiders.

With the SEC intent on developing novel and aggressive ways to fight insider trading, it should come as no surprise that it strongly supports a new approach proposed by several securities self regulatory organizations (SROs). On August 18, 2008, the SEC announced that several SROs¹ had developed an agreement to create a centralized system of insider trading surveillance and detection similar to the Options Regulatory Surveillance Authority Plan (ORSAP) that was created by several SROs² in 2006 to detect insider trading involving securities options. The SROs' proposed agreement is still in the public comment phase, with comments due September 8 and none submitted so far. Serious objection to this agreement seems unlikely, as an initial request for comments about the ORSAP elicited no public comments. Thus, it can be expected that the SEC will approve the SROs' agreement.

The SROs' agreement calls for a system in which surveillance, investigation and enforcement of insider trading by broker dealers and their associated persons across all the equities markets is centralized under NYSE Regulation, Inc. and FINRA. NYSE Regulation would oversee the SROs' agreement with respect to common Members trading NYSE and NYSE Arca listed securities, and FINRA would be responsible for common Members trading NASDAQ and American Stock Exchange listed securities and securities listed exclusively on the Chicago Stock Exchange. Although all of the exchanges will share the costs of operating the system, no individual exchange will retain any right to conduct its

¹ The following ten equity exchanges, in addition to FINRA and NYSE Regulation (acting under the authority given to it by the NYSE), are parties to the SROs' Agreement: the American Stock Exchange, Boston Stock Exchange, CBOE Stock Exchange, Chicago Stock Exchange, International Securities Exchange, NASDAQ, National Stock Exchange, NYSE, NYSE Arca, and the Philadelphia Stock Exchange.

² The following six exchanges are parties to the ORSAP: the American Stock Exchange, Boston Stock Exchange, Chicago Board Options Exchange, International Securities Exchange, Pacific Exchange (now, NYSE Arca) and the Philadelphia Stock Exchange.

own insider trading detection activities or take disciplinary actions against its own members for insider trading violations.

The SEC believes this plan will permit the securities exchanges to more efficiently track and identify cases of insider trading and will merge repetitive investigations now conducted by each individual exchange into one centralized and cohesive system. Consequently, it will be easier to identify instances of insider trading, making the SEC's goal of punishing persons who manipulate the equities markets even more viable.

Insider trading is one of the oldest securities crimes and continues to be a persistent problem. Whether the SROs' agreement will in fact contribute to a lessening of insider trading violations is not yet clear when viewed against the backdrop of the ORSAP. While the SEC has voiced enthusiasm about the ORSAP, since in its inception in 2006, the only real evidence of its contributions to fighting insider trading appears in two SEC litigation releases in March and July 2008 where the SEC acknowledged the assistance of the ORSAP. What is clear is that the SEC is becoming ever more innovative and aggressive in combating the crime of insider trading and upholding its responsibility to oversee the implementation of progressive solutions where SROs fail.

Natasha Meruelo is an attorney at The Nelson Law Firm in White Plains, N.Y.