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THE EEC DIRECTIVE ON INSIDER TRADING: WILL THERE BE A CURE BY 1992?

Thomas J. Ramsdell*

"If one adopts the point of view of a common European securities market, rather than looking at what happens on a country by country basis, the situation cannot be said to be satisfactory unless all the constituent elements of the market are functioning efficiently and in a broadly equivalent way."¹

INTRODUCTION

The internationalization² of the world's securities markets, a new phenomenon,³ has markedly transformed financial markets. Increased concern for preserving the integrity of the markets through regulation of insider trading is one of the most visible manifestations of this new internationalization.⁴

Varied and complex forces underlie the internationalization of the world securities markets.⁵ The advance of technology is the most important influence in the recent trend toward market integration.⁶ This

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1. Cruickshank, *Insider Trading in the EEC*, 10 INT'L BUS. LAW. 345, 346 (1982).

2. See Comment, *Insider Trading and the Internationalization of the Securities Markets*, 27 COLUM. J. TRANSNAT'L L. 409, 409 (1989) [hereinafter Comment, *Internationalization of the Securities Markets*] (discussing the common usage of the word "internationalization" to describe recent developments in the attempt to control insider trading on the international level). Integration more accurately describes the current situation, as world securities markets have established linkages such as stock quotation sharing with the United States market. *Id.* at 411-15.

3. See Regulation of International Securities Markets, Exchange Release No. 33-6807, 53 Fed. Reg. 46,963 (Nov. 14, 1988) [hereinafter SEC Regulation] (stating that international securities markets have grown substantially over recent years).

4. See *id.* at 13-14 (noting that regulators should strive for efficiency and fairness in the world's security market system through regulation of insider trading and market fraud).

5. See Kubler, *Regulatory Problems in Internationalizing Trading Markets*, 9 U. PA. J. INT'L BUS. L. 107, 107 (1987) (stating that the complexity of the international securities markets tends to foster regulatory problems).

6. See Grunson, *The Global Securities Market: Introductory Remarks*, 1987 COLUM. BUS. L. REV. 303, 305 (1987) (stating that advances in modern technology have fostered global expansion of securities markets technology); see also Comment, *Internationalization of the Securities Markets*, *supra* note 2, at 410-11 (stating that technological advances have strongly affected the modernization of the internationalization process); Peters & Feldman, *The Changing Structure of the Securities Markets and the Securities Industry: Implications for International Securities Regulation*, 9 MICH. Y.B. INT'L. LEGAL STUD. 19, 21 (1987) (stating that the speed, accuracy, and

new technology gives investors and market professionals the ability to trade securities on virtually every national exchange in the world, thus opening a vast new window of opportunity.⁷

The benefits of economic interdependence and a diversified portfolio are major factors in world market integration.⁸ American investors and businesspersons anxiously seek to take advantage of higher returns in foreign markets⁹ and the various European privatization programs that have afforded great investment opportunities.¹⁰ Finally, numerous other factors, including the need for capital fostered by third world development,¹¹ the relaxation of foreign exchange controls,¹² and the demands

efficiency in transmitting information allowed investors to make investment decisions more easily, permitting both investors and issuers to make use of information from all global markets).

7. See Comment, *Internationalization of the Securities Markets*, *supra* note 2, at 411 (discussing the execution of trades in technologically advanced markets). The ability to monitor price movements and quotations around the globe is the most important aspect of the technological advance in securities regulation. *Id.* This allows an investor to monitor all price quotations for an internationally listed stock and to execute a transaction based upon the best market price. *Id.*

8. See *id.* at 409-10 (stating that one can reduce risk in an era of uncertain markets through portfolio diversification). The Securities and Exchange Commission states that international investment diversification provides an element of risk reduction that domestic investment alone cannot achieve. SECURITIES & EXCHANGE COMMISSION, INTERNATIONALIZATION OF THE SECURITIES MARKETS, REPORT OF THE STAFF OF THE U.S. SECURITIES AND EXCHANGE COMMISSION TO THE SENATE COMM. ON BANKING, HOUSING AND URBAN AFFAIRS AND THE HOUSE COMM. ON ENERGY AND COMMERCE II-4 (July 27, 1987).

9. See Sloane, *The Lure of Investing Abroad*, N.Y. Times, Aug. 11, 1987, at D1 (stating that many United States investors take advantage of stronger foreign markets and currencies). In United States dollar terms, during the 18 month period between December 31, 1985 and July 31, 1987, the Mexican market gained 543.83%, the Spanish market gained 183.74%, the Singapore market gained 130.84%, the Japanese market gained 167.46%, and the Hong Kong market gained 110.52%. *Id.* The United States market gained 47.40% during the same period. *Id.*

10. See Peters & Feldman, *supra* note 6, at 21-22 (discussing various European privatization programs). The United Kingdom and France have had several successful public stock offerings with significant foreign investor participation. *Id.* at 22. Some examples of these multinational common stock offerings in the United Kingdom include the \$12 billion sale of British Petroleum, the \$8 billion sale of British Gas, the \$5 billion sale of British Telecom, and the \$2.3 billion sale of Rolls Royce. *Id.* at 22 n.9. France has sold some of its stock, and has urged its citizens to become stockholders. N.Y. Times, May 8, 1987, at 15.

11. See Note, *Toward the Unification of European Capital Markets: The EEC's Proposed Directive on Insider Trading*, 11 FORDHAM INT'L L.J. 432, 434 (1988) [hereinafter Note, *Toward the Unification*] (stating that third world debt has contributed to the worldwide demand for capital); Kubler, *supra* note 5, at 110-11 (stating that an increased demand for capital created by the needs of developing nations has fostered the internationalization process).

12. See Kubler, *supra* note 5, at 110 (stating that lesser controls on foreign exchanges has helped ease the movement of capital between markets).

of industrialized societies,¹³ have added to the internationalization process.¹⁴

While the factors contributing to the integration of the world securities markets are important, the implications of this process are paramount. The international securities markets are now interdependent.¹⁵ As a result, a prospective investor can trade on the exchanges virtually twenty-four hours a day from anywhere in the world.¹⁶ This presents an irony, as the same technologies that helped to develop a global securities market also have created the opportunity for international fraud.¹⁷

This Comment will explore one of the most visible practices implicated by increasingly internationalized securities markets—insider trading. Specifically, the Comment will address the issue of insider trading in Europe in light of the internationalization process and the prospect of unified financial markets in the European Economic Community (EEC or the Community) by 1992. Two EEC Member-States, Great Britain and Germany, have addressed the issue of insider trading in virtually opposite ways. By analyzing their insider trading regulations with the recent EEC directive on insider trading, this Comment will shed light on the prospects for substantive regulation of the world's securities markets.

13. See Note, *Toward the Unification*, *supra* note 11, at 434 (stating that the economic growth of industrialized nations has, among other factors, contributed to the demand for capital); Kubler, *supra* note 5, at 111 (stating that budget deficits in leading industrialized countries create a demand for capital).

14. See *Internationalization of the Securities Markets*, *supra* note 2, at 411-13 (giving statistical breakdowns of the amounts of capital involved and the percentage change in investment patterns of the various securities markets); Note, *Toward the Unification*, *supra* note 11, at 434-35 (discussing the large increase in international trade volumes over recent years); Kubler, *supra* note 5, at 107-10 (noting various trends in the expansion of security trading); Peters & Feldman, *supra* note 6, at 22-24 (illustrating the internationalization of the international securities markets); Request for Comments on Issues Concerning Internationalization of the World Securities Markets, Exchange Act Release No. 34-21958, 15 Fed. Reg. 16,302 (Apr. 18, 1985) (discussing various reasons for the internationalization process).

15. See Peters & Feldman, *supra* note 6, at 20, 37 (noting the interdependence of the world securities markets, and illustrating this by analyzing the October 1987 market break in an international context).

16. See *supra* notes 6-7 and accompanying text (discussing the technological advances that have fostered around-the-clock international securities markets).

17. See Fedders, *Policing Trans-Border Fraud in the United States Securities Markets: The "Waiver-by-Conduct" Concept—A Possible Alternative or a Starting Point for Discussions?*, 11 BROOKLYN J. INT'L L. 477, 494-95 (1985) (commenting that the new world economic order lends itself to business fraud).

I. INTERNATIONALIZATION AND INSIDER TRADING

While the recent integration of the securities markets has created substantial investment opportunities for prospective investors,¹⁸ it also has exposed deficiencies in market regulation capabilities.¹⁹ The disparate degree of protection that the international investor receives in the global marketplace most clearly illustrates these deficiencies.²⁰ For example, of the twelve member States comprising the European Economic Community,²¹ only Great Britain, France, and Denmark have codified prohibitions against insider trading.²²

In addition, the differences between legal structures²³ and behavioral attitudes²⁴ in the various national systems create specific regulatory problems.²⁵ The varying degrees of market regulation and investor pro-

18. See *supra* notes 6-10 and accompanying text (discussing how modern technology has created new opportunities for the international investor).

19. See SEC. & EXCH. COMM'N POLICY STATEMENT OF THE UNITED STATES SECURITIES AND EXCHANGE COMMISSION: REGULATION OF INTERNATIONAL SECURITIES MARKETS, INTERNATIONAL SERIES RELEASE NO. 14 (Nov. 1988) [hereinafter POLICY STATEMENT] (discussing the inadequacies of the present regulatory system). Present regulatory systems cannot keep pace with a 24-hour per day global trading scheme, as quotation, price, and volume information is usually only available at the end of a trading day, or at fixed times during the day. *Id.* This effectively prevents the efficient operation of the capital markets. *Id.*

20. See Note, *Toward the Unification*, *supra* note 11, at 435 (commenting that some regulatory provisions require strict enforcement, while some do not provide any insider restrictions); see also Carlton & Fischel, *The Regulation of Insider Trading*, 35 STAN. L. REV. 857, 860 (1983) (stating that various national markets traditionally have not regulated or enforced existing regulations).

21. See *Common Market in Profile*, 1 COMMON MKT. REP. (CCH) ¶ 101.07 (June 18, 1987) (noting that the 12 member-states of the EEC are: Belgium, France, West Germany, the Netherlands, Italy, Luxembourg, the United Kingdom, Ireland, Denmark, Greece, Spain, and Portugal).

22. Nieuwdorp, *EEC Harmonization Report*, 16 INT'L BUS. LAW. 39, 42 (1988). The Netherlands, Belgium, and Ireland are considering legislation, while the Federal Republic of Germany requires market professionals to observe a private civil code of conduct. *Id.*

23. See Kubler, *supra* note 5, at 113 (stating that differences in regulations may stem from differences in the structure of each country's existing system). A country's private law traditions influence its substantive rules. *Id.* The problems associated with automated settlement procedures reflect this influence. *Id.* For example, the United States solves the problem through a trust relationship, while German settlement procedures depend upon domestic property law. *Id.*

24. *Id.* at 115. Enforcement efforts and sanctions imposed depend upon the national philosophy of fairness in the distribution of corporate earnings between company fiduciaries and investors. *Id.* For example, a country may not actively enforce insider trading regulations if a concern for customer-broker confidentiality outweighs the concern for policing insider trading. *Id.*

25. See *id.* at 112 (stating that varied treatment of the same situation in different countries fosters international regulatory problems).

tection threaten the efficiency of the markets²⁶ and undermine their integrity.²⁷ Potentially, investor decline and fraud will result.²⁸

Finally, some speculate that developing a coordinated regulatory system that will harmonize the insider trading regulations of the various national markets is in the European Community's best interest.²⁹ In fact, the former Director of the Division of Enforcement at the Securities and Exchange Commission (SEC) has commented that each foreign market has an interest in preventing its investors from being exposed to a high level of protection in the home market and a reduced level of protection on a foreign exchange.³⁰ Although the process has been slow and the outcomes are at best uncertain, over the past twenty years several European countries have gradually moved towards stricter insider trading prohibitions.³¹ In 1989, the EEC adopted a uniform set of provisions for the regulation of insider trading in the member-states.³²

26. See POLICY STATEMENT, *supra* note 19, at 12 (noting that regulatory measures should work to promote market efficiency).

27. See Comment, *Internationalization of the Securities Markets*, *supra* note 2, at 419 (stating that most United States commentators recognize that insider trading frustrates the integrity of the market); Note, *Toward the Unification*, *supra* note 11, at 436 (stating that the "proper functioning" of the market depends on investor confidence).

28. POLICY STATEMENT, *supra* note 19, at 12. The SEC has supported its call for fair and honest markets through uniform regulation by stating that:

Investors will seek out markets they perceive as fair and honest. Countries that do not have prohibitions against insider trading, market manipulation, and misrepresentations to the marketplace risk becoming havens for illegal activities. Market abuses result in less efficient markets, higher insurance and other costs and, most important, the absence from those markets of individual and institutional investors who consider integrity to be an essential market characteristic.

Id.

29. See Kubler, *supra* note 5, at 112 (speculating that if the various nations adopted a uniform set of laws they could eradicate problems caused by inconsistent regulations).

30. G. Lynch, Address to Financial Times International Conference on Developing the Global Market for Equities 6 (Oct. 21, 1986) (quoted in *Internationalization of the Securities Markets*, *supra* note 2, at 437 n.171).

31. See Peters & Feldman, *supra* note 6, at 33-34 (describing various legislative initiatives in the United Kingdom, France, Sweden, the Netherlands, Switzerland, Italy, Belgium, Denmark, and Ireland).

32. Council Directive Coordinating Regulations on Insider Dealing, O.J. E.C.R. COMM. (No. L 334) 30 (1989) [hereinafter *Council Directive*].

II. THE REGULATION OF INSIDER TRADING IN THE EUROPEAN ECONOMIC COMMUNITY

A. ECONOMIC GOALS OF THE EEC

The occurrence of fraud and insider trading negatively affects the integrity and efficiency of capital markets.³³ The EEC's desire to curb this harmful practice is rooted in one of the four "freedoms" spelled out by the Treaty of Rome³⁴—the freedom of movement of capital.³⁵ Inherent in the free movement of capital is the establishment of a common capital market in the Community.³⁶ In turn, the EEC believes that interpenetration of the national markets is the most effective way to achieve this goal.³⁷ Thus, it is clear that if markets afford unequal protection to investors, investors will withdraw from the markets and the interpenetration process will be frustrated.³⁸ As a result of this inevitable market decline, it became crucial for the EEC to ensure that member States observe satisfactory standards of investor protection.³⁹ Because the Treaty of Rome allows the EEC to create certain safeguards in the interest of uniformity and protection of each Member State,⁴⁰ in 1987 the Community took its first substantive step towards equalizing investor protection by adopting a draft directive on insider

33. See notes 25-28 and accompanying text (illustrating the importance of efficiency and integrity in the international markets).

34. Treaty Establishing the European Economic Community, Mar. 25, 1957, 1973 Gr. Brit. T.S. No. 1 (Cmd. 5179-II) (official English trans.), 298 U.N.T.S. 11 (1958) (unofficial English trans.) [hereinafter Treaty of Rome].

35. *Id.* at 15-16. Article 3(c) of the Treaty of Rome advances the goal of obtaining the free movement of capital throughout the Community. *Id.* The article states that the Community should actively abolish obstacles to free movement for people, money and service, among Member States. *Id.*

36. See Cruickshank, *supra* note 1, at 346 (stating that the creation of a common capital market is inherent in the "freedom of movement of capital" as set forth in the Treaty of Rome).

37. *Press Release from the Commission of the European Communities*, 4 COMMON MKT. REP. (CCH) § 10,880 (Apr. 28, 1987) [hereinafter *Press Release*].

38. See Comment, *Securities—Insider Trading—The Effects of the New EEC Draft Insider Trading Directive*, 18 GA. J. INT'L & COMP. L. 119, 132 (1988) [hereinafter Comment, *New EEC Draft Directive*] (discussing the importance of uniform investor protection in the interpenetration process); POLICY STATEMENT, *supra* note 19, at 12 (noting that honest markets will attract investors and dishonest ones will drive them away).

39. Cruickshank, *supra* note 1, at 346.

40. See Schneebaum, *The Company Law Harmonization Program of the European Community*, 14 LAW & POL'Y INT'L BUS. 293, 296 (1982) (explaining the use of safeguards to foster protection of the member-states' interests). The relevant sections of the Treaty of Rome are arts. 83-130, 298 U.N.T.S. at 47-66.

trading.⁴¹ It finalized this initiative on November 13, 1989, by adopting the Council Directive Coordinating Regulations on Insider Dealing (the Directive).⁴²

EEC involvement in insider trading regulation stems from the realization that insider trading is a real and growing problem. The chronic phenomenon of significant price movement in stock prices prior to major corporate developments best indicates the insider trading problem.⁴³ Furthermore, the national markets are becoming increasingly internationalized, and the insider trading regulations of each of the twelve Member States are inconsistent.⁴⁴ In order to meet the goals set forth in the Single European Act,⁴⁵ which include the formation of a large and integrated market by 1992,⁴⁶ it is clear that the EEC will have to overcome those obstacles which threaten the smooth operation of the national securities markets.⁴⁷

41. *Proposal for a Council Directive Coordinating Regulations on Insider Trading*, 10 O.J. EUR. COMM. (No. C 153) 8 (1987) [hereinafter *Draft Directive*].

42. *Council Directive*, *supra* note 32.

43. See Hawes, Lee & Robert, *Insider Trading Law Developments: An International Analysis*, 14 LAW & POL'Y INT'L BUS. 335, 336 (1982) (suggesting that such price movement is indicative of the deficiencies in laws governing insider trading and enforcement).

44. See *supra* notes 5-17, 20-25 and accompanying text (discussing the internationalization process and the inconsistency of national legislation in the Member States).

45. *Single European Act*, O.J. EUR. COMM. (No. L 169) 1 (1987) [hereinafter *Single European Act*], amending Treaty Establishing the European Economic Community.

46. *Id.* The Single European Act states, in relevant part:

Article 130a

In order to promote its overall harmonious development, the Community shall develop and pursue its actions leading to the strengthening of its economic and social cohesion.

In particular the Community shall aim at reducing disparities between the various regions and the backwardness of the least-favoured regions.

Article 130b

Member States shall conduct their economic policies, and shall coordinate them, in such a way as, in addition, to attain the objectives set out in Article 130a. The *implementation of the common policies of the internal market* shall take into account the objectives set out in Article 130a and in 130c and shall contribute to their achievement.

Id. at 9 (emphasis added).

47. See Fornasier, *The Directive on Insider Dealing*, 13 FORDHAM INT'L L.J. 149 (1989-1990) (stating that insider trading is a problem that the EEC must correct in order to bring about proper functioning of the market). The author also suggests that recent insider trading cases and scandals have taken on political consequence and have thus added to the need for a quick and uniform solution to the problem. *Id.* at 149-50.

B. THE COMPANY LAW HARMONIZATION PROGRAM AND THE DIRECTIVE PROCESS

A central aspect of the Treaty of Rome combines the goal of free movement of persons, services, and capital among the Member States into what is termed "the right of establishment."⁴⁸ This right includes the right of a national company of one Member State to conduct business in any other Member State.⁴⁹ To provide for more effective realization of this goal, the Treaty of Rome grants the EEC the power to create equivalent protective safeguards among the Member States.⁵⁰ To this end, the EEC encourages Member States to harmonize legislation in order to reduce high levels of risk to shareholders and potential investors.⁵¹

The Treaty of Rome grants the European Community Council of Ministers the power to issue directives to the Member States.⁵² The Community employs EEC directives to harmonize the laws of the Member States, by forcing them to adopt national legislation consistent with the directive.⁵³ The Council established a directive in an effort to

48. See Schneebaum, *supra* note 40, at 295-96 (explaining the elements of the "right of establishment").

49. Treaty of Rome, *supra* note 34, art. 52.

50. *Id.* art. 54, para. 3(g).

51. See Schneebaum, *supra* note 40, at 296 (discussing investor protection through harmonization).

52. Treaty of Rome, *supra* note 34, art. 54(2). The Treaty of Rome states that: In order to implement the general programme, or if no such programme exists, to complete one stage towards the achievement of freedom of establishment for a specific activity, the Council, on a proposal of the Commission and after the Economic and Social Committee and the [Parliament] have been consulted, shall, until the end of the first stage by means of a unanimous vote and subsequently by means of a qualified majority vote, act by issuing directives.

Id.

53. Schneebaum, *supra* note 40, at 296. The directive is binding "as to the result to be achieved, while leaving to domestic agencies a competence as to form and means." Treaty of Rome, *supra* note 34, art. 189.

The Treaty of Rome affords the Commission the authority to introduce a new proposal. Treaty of Rome, *supra* note 34, art. 54(2). Once a proposal is introduced, the Commission appoints a "working party" to study it and make appropriate recommendations. II.A INTERNATIONAL ORGANIZATION AND INTEGRATION at Dir. 20-22 (1982) [hereinafter INTERNATIONAL ORGANIZATION]. Following this process, which can take several years, the Commission drafts a version of the proposal and sends it to the Council. Treaty of Rome, *supra* note 34, art. 54(2). According to the Treaty of Rome, before the Council can act on the proposal, it must consult with the European Parliament and the Economic and Social Committee. *Id.* at 193-98. The European Parliament consists of representatives from each Member State. INTERNATIONAL ORGANIZATION, *supra*. Unlike the members of the Council, Parliament members do not represent a particular Member State's national government. *Id.* The European Parliament's primary purpose is to issue advisory opinions to the Council. *Id.* Essentially, the Economic and Social Committee acts in an advisory capacity. Treaty of Rome, *supra* note 34,

bring the Member States' insider trading regulations of the Member States into conformity.

C. HISTORY OF THE DIRECTIVE ON INSIDER TRADING

The 1977 European Code of Conduct was the EEC's first effort to address insider trading.⁵⁴ This voluntary code provided that any person in possession of privileged or price sensitive information while acting within the scope of his or her employment should refrain from dealing in that particular security or disclosing price sensitive information.⁵⁵ The Code was an early attempt to address insider trading. The actual Directive process began in 1982, however, when the Commission assembled a group of experts to determine the need for establishing further regulation of the securities markets of the EEC Member States.⁵⁶ The experts believed that interpenetration of the capital markets required at least minimum standards of uniform investor protection.⁵⁷ Insider trading regulations, therefore, were a necessary element of any effective protective measures.⁵⁸

On April 28, 1987, the Commission adopted the Proposal for a Council Directive Coordinating Regulations on Insider Trading (Draft

art. 54(2). The Committee represents workers, employees, and consumer interests. *Id.* The Economic and Social Committee receives the proposal only if it involves economic concerns. *Id.* Once the European Parliament and the Economic and Social Committee evaluates the proposal, if there are any additional proposals or changes, the Commission must consider them. Schneebaum, *supra* note 40, at 297.

The Council of Ministers is responsible for the next and final mediation phase, generally consisting of three stages. *Id.* at 298. The first level is basically a "working party" of specialists. *New EEC Draft Directive, supra* note 38, at 131. As representatives of the various ministries of the Member States, the Council of Ministers reviews the elements of the proposal and attempts to overcome technical hurdles to the Council's final adaptation. Schneebaum, *supra* note 40, at 298. Second, the Committee of Permanent Representatives, which consists of members of ambassadorial standing from each of the Member States, considers the political ramifications of the proposal. *Id.* Finally, the Foreign Ministers of each of the Member States, the Council of Ministers, considers the proposal put before it, and has the power to adopt the Directive and to give it full legal effect. Treaty of Rome, *supra* note 34, art. 100a.

54. *European Code of Conduct Relating to Transactions in Transferable Securities*, O.J. EUR. COMM. (No. L 212) 41 (1977).

55. *Id.* See generally B. RIDER & H. FRENCH, *THE REGULATION OF INSIDER TRADING* 268-71 (1979) (discussing the Code of Conduct).

56. See Cruickshank, *supra* note 1, at 346 (discussing the state of insider regulations in 1982). At this time the Commission was evaluating to what extent it should initiate further programs through the directive procedure. At that time, the Council adopted three directives relating to stock exchange issues. *Id.*

57. See *supra* note 38 and accompanying text (discussing the interpenetration process and the need for uniform investor protection).

58. Cohen, *Toward an International Securities Market*, 5 LAW & POL'Y INT'L BUS. 357, 390 (1973).

Directive).⁵⁹ The Commission submitted the Draft Directive to the Council on May 25, 1987.⁶⁰ Remarkably, only twenty-nine months later, the Council adopted the Directive.⁶¹

D. THE INSIDER TRADING DIRECTIVE

1. Goals of the Directive

The legislative intent of the EEC Insider Trading Directive illustrates some of the goals of the directive. As the debates and various committee reports that take place during the course of EEC legislation are not part of the public record, the history of EEC legislation cannot be analyzed in the same way as legislative history in the United States. The preamble of the Directive, however, enumerates the economic goals the Council sought to realize by adopting this particular legislation.⁶²

The creation and smooth functioning of the internal market in the EEC is the primary aim of the insider trading directive.⁶³ Through the Directive, the Council, using its authority under Article 100a of the Treaty of Rome,⁶⁴ sought to promote investor confidence and protection and the successful interpenetration of the national markets.⁶⁵ The

59. Draft Directive, *supra* note 41.

60. *Id.*

61. *Council Directive, supra* note 32. Many consider the 29 month adoption period to be comparatively short when measured against other Community legislative initiatives. See Fornasier, *supra* note 47, at 152 (stating that the 29 month adoption period is considered short by EEC legislative standards).

The relative ease with which the directive moved through the EEC legislative process strongly indicates that the Member States recognize the importance of uniform market regulation. The EEC may, therefore, implement the Directive rather quickly and enforce it more stringently than other EEC stock market initiatives.

62. *Council Directive, supra* note 32, preamble.

63. *Id.* The preamble of the Directive states:

Whereas Article 100a (1) of the Treaty [of Rome] states that the Council shall adopt the measures for the approximation of the provisions laid down by law, regulation or administrative action in Member States which have as their object the establishment and functioning of the internal market. *Id.*

64. *Id.*

65. *Council Directive, supra* note 32, preamble. An additional section of the Directive's preamble states in relevant part:

Whereas the secondary market in transferable securities plays an important role in the financing of economic agents;

Whereas, for that market to be able to play its role effectively, every measure should be taken to ensure that market operates smoothly;

Whereas, the smooth operation of that market depends to a large extent on the confidence it inspires in investors;

Whereas the factors on which such confidence depends include the assurance afforded to investors that they are placed on an equal footing and that they will be protected against the improper use of inside information;

Council believed that it could not accomplish the smooth functioning of the internal markets without uniform regulation of insider trading.⁶⁶

The Council's Statement to the Parliament contained in the Amended Proposal demonstrates a second policy consideration behind the adoption of the Directive.⁶⁷ In this statement, the Council clearly articulated the goals of insider trading regulation.⁶⁸ These aims entail balancing supply and demand with equal opportunity for all investors by prohibiting individuals with inside information from taking advantage of this information at the expense of other market players.⁶⁹ Additionally, the Council stated that the attempt to reach a uniform level of investor protection stemmed from the significant differences in the ways that those Member States which regulate insider trading approach the issue, and from the fact that several Member States do not regulate insider trading at all.⁷⁰ The ultimate goal of the Directive, therefore, is to harmonize the insider trading provisions of the Member States and provide a uniform level of protection to capital market investors.⁷¹

2. *The Directive's Definitions and Scope*

The Directive, as with most laws dealing with insider trading, contains two central definitions: "inside information" and "insider."⁷² It

Whereas, by benefiting certain investors as compared with others, insider dealing is likely to undermine that confidence and may therefore prejudice the smooth operation of the market;

Whereas the necessary measures should therefore be taken to combat insider dealing;

Whereas in some Member States there are no rules or regulations prohibiting insider dealing and whereas the rules or regulations that do exist differ considerably from one Member State to another;

Whereas it is therefore advisable to adopt coordinated rules at a Community level in this field;

Whereas such coordinated rules also have the advantage of making it possible, through cooperation by the competent authorities, to combat transfrontier insider dealing more effectively

Id.

66. *Id.*

67. Fornasier, *supra* note 47, at 150 n.5 (citing *Common Position Adopted by the Council on July 18, 1989 with a View to the Adoption of a Directive Coordinating Regulations on Insider Dealing*, EUR. PARL. SESS. DOCS., ser. C, doc. C 3-0018/89 (July 28, 1989) [hereinafter *Amended Proposal*]).

68. *Id.*

69. *Id.*, *Amended Proposal*, at 2-3.

70. *Id.*

71. *Supra* notes 36-39 and accompanying text (discussing equal protection of market investors).

72. *Council Directive*, *supra* note 32, arts. 1 & 2.

defines inside information broadly.⁷³ While incorporating the British and West German definitions,⁷⁴ the Directive sets forth four elements that describe "inside" information. These elements are: 1) non-public information; 2) relating to issuers or issues of transferable securities; 3) likely to have a material effect on the price of the security if published; 4) of an exact nature.⁷⁵ Although parts of the Directive's definition of inside information may be susceptible to judicial interpretation,⁷⁶ one can speculate that it will gain acceptance throughout the Community because the Directive draws from the language of the British and West German insider trading regulations⁷⁷ and is also similar to the French insider trading provisions.⁷⁸

The definition of "insider," like the definition of inside information, has a broad scope.⁷⁹ Most significantly, the definition includes both "primary" and "secondary" insiders.⁸⁰ The Council thus chose the

73. See *New EEC Draft Directive*, *supra* note 38, at 136 (demonstrating the breadth of the Directive's definition of insider trading); Note, *Toward the Unification*, *supra* note 11, at 448 (describing the Directive's definition as thorough).

74. See *New EEC Draft Directive*, *supra* note 38, at 136 (noting that the EEC definition of inside information coincides with the definition in the United Kingdom and West Germany).

75. *Council Directive*, *supra* note 32, art. 1. The Directive provides in relevant part:

1. "inside information" shall mean information which has not been made public of a precise nature relating to one or several issuers of transferable securities or to one or several transferable securities, which, if it were made public, would be likely to have a significant effect on the price of the transferable security or securities in question

Id.

76. See *New EEC Draft Directive*, *supra* note 38, at 136 (stating that certain words such as "unknown" and "material" may be subject to judicial interpretation).

77. *Id.*

78. See Comment, *Insider Trading and the EEC: Harmonization of the Insider Trading Laws of the Member States*, 7 B.C. INT'L & COMP. L. REV. 151, 174 (1985) [hereinafter Comment, *Harmonization of the Member States*] (stating that the Directive's definition of inside information is similar in some respects to the French definition).

79. See Comment, *New EEC Draft Directive*, *supra* note 38, at 133 (stating that the definition of insider is broad and all-encompassing); Note, *Toward the Unification*, *supra* note 11, at 448 (stating that the broad definition of insider is one of the Directive's strongest assets).

80. *Council Directive*, *supra* note 32, arts. 2, ¶ 1, 4. The Directive provides, in relevant part:

Article 2

1. Each Member State shall prohibit any person who:

—by virtue of his membership of the administrative, management or supervisory bodies of the issuer,

—by virtue of his holding in the capital of the issuer, or

—because he has access to such information by virtue of the exercise of his employment, profession or duties, possesses inside information from taking advantage of that information with full knowledge of the facts by acquiring or dispos-

broadest commonly accepted definition of insider, including the "company professional" (tipper) and the person who knowingly uses the privileged information (tippee).⁸¹ This choice of definitions is important, for if the EEC truly seeks to eradicate the practice of insider trading, it should prohibit anyone with privileged information from trading on that knowledge. This expansive definition of insider ensures investors' confidence in the securities market.⁸² Finally, the language of the Directive does not lend itself to legislative or judicial manipulation. The Directive provides adequately specific boundaries to prevent individual Member States or the courts from altering the definitional scope or intent.⁸³

Aside from the definitions of insider and inside information, additional restrictive components of the Directive further explicate the scope of the Directive. The first and most widely recognized restriction is that any person whom the Directive covers may not trade any transferable security⁸⁴ on a national market within the territory of a particu-

ing of for his own account or for the account of a third party, either directly or indirectly, transferable securities of the issuer or issuers to which that information relates.

Article 4

Each Member State shall also impose the prohibition provided for in Article 2 on any person other than those referred to in that Article who with full knowledge of the facts possesses inside information, the direct or indirect source of which could not be other than a person referred to in Article 2.

Id.

81. See Cruickshank, *supra* note 1, at 346-47 (delineating three definitional alternatives for insider available to the law makers); see also Note, *Toward the Unification*, *supra* note 11, at 448 (stating that a narrower approach would have left out the tippees, and that effective legislation would have to include any person who knowingly trades on the basis of privileged information); Comment, *New EEC Draft Directive*, *supra* note 38, at 133 (applauding the definition for its breadth and specificity).

Only the United Kingdom employed this inclusive definition of insider, which includes both tipplers and tippees. At least one commentator believes such a definition is too expansive because it creates the possibility of an endless chain of insiders. Cruickshank, *supra* note 1, at 347.

82. See Note, *Toward the Unification*, *supra* note 11, at 448 (stressing the importance of involving the tippee in the Directive's definition of insider as opposed to merely including the fiduciaries of the company in question).

83. See Fornasier, *supra* note 47, at 163-64 (arguing that the Council definition of insider trading is so stringent that each Member State will have to implement uniform definitions). But see *New EEC Draft Directive*, *supra* note 38, at 133-34 n.110 (arguing that there are some words, such as "professional," "duties," and "in the exercise of" which might undergo judicial interpretation that would alter the meaning of insider).

84. See *Council Directive*, *supra* note 32, art. 1(2) (defining transferable securities). Transferable securities include shares, debt securities, contracts or rights to subscribe, acquire, or dispose of securities, index contracts, and futures. *Id.*

lar Member State.⁸⁶ Second, it is important to note that just as the Directive prevents a person from dealing on the basis of inside information, a company or legal person is prohibited from such transactions.⁸⁶ Third, the Directive does not prevent tippees from disclosing privileged information to third parties.⁸⁷ Finally, the prohibitions against insider dealing apply to transactions carried out through a professional intermediary, such as a bank, holding company, or stock-broker.⁸⁸

3. Implementation

One of the unique features of a Council Directive is its adaptability. Once the Council passes a Directive, the Member States usually have a two year period in which to bring their national legislation into conformity with its provisions.⁸⁹ Thus, a Directive is not a *per se* "binding instrument."⁹⁰ In keeping with this distinctive method of legislation, the insider trading Directive provides that each Member State must comply with its requirements on or before June 1, 1992.⁹¹ This obligates each Member State to inform the Commission when the appropriate measures have been taken and what provisions their individual national legislatures have adopted.⁹²

85. *Council Directive, supra* note 32, art. 5. Article 5 of the Directive applies only to issues and issuers dealing in transferable securities within the territory of the Member State. *Id.* The Directive, however, does not regulate transactions that take place outside the territory of a particular national exchange. *New EEC Draft Directive, supra* note 38, at 137. While this limitation may seem contrary to the notion of promoting Community wide investor protection, to the extent that not all Member States are in agreement regarding how far reaching the prohibitions should be, Article 5 may represent a compromise position. *Id.* at 138. It is important to understand that with all of the provisions set forth, a Member State may adopt more stringent rules, thus determining whether or not it wishes to extend regulation over markets outside of its territory. Fornasier, *supra* note 47, at 164-65.

86. *Council Directive, supra* note 32, art. 2 (2).

87. One can derive this interpretation from Article 6, which allows a Member State to *extend* its national laws to include prohibitions against tippees disclosing insider information. *See* Comment, *New EEC Draft Directive, supra* note 38, at 138 (explaining how the Directive focuses on the tipper, not the tippee).

88. *Council Directive, supra* note 32, art. 2(3). A Member State, however, may suspend the prohibition against the use of insider information in cases dealing outside of the national market, not carried out through a professional intermediary. *Id.*

89. *See* Cruickshank, *supra* note 1, at 345 (stating that directives are flexible because the national authorities are free to choose their own method of implementation); *see also* Fornasier, *supra* note 47, at 162 (stating that Member States are able to choose the legal means to attain a directive's goal); Comment, *New EEC Draft Directive, supra* note 38, at 130 (stating that a directive is not binding as to the implementation of the means, but only as to the result in achieving its stated goal).

90. *See supra* note 89 and accompanying text (discussing the flexibility and purposes of the Directive's implementation scheme).

91. *Council Directive, supra* note 32, art. 14.

92. *Id.*

In order to give additional credence to the requirements of a council directive, the Court of Justice strictly interprets the term implementation.⁹³ As such, *de facto* compliance with the Directive provisions is insufficient.⁹⁴ A Member State must expressly bring its national legislation into compliance with the Directive.⁹⁵ While the United Kingdom, France, and Denmark have criminal statutes prohibiting insider trading, the other Member States, including Germany, do not.⁹⁶ This disparity suggests that most Member States will have to significantly alter their historical approach to insider trading by adopting an entirely new set of laws.

4. Enforcement

Perhaps the most important, and certainly some of the most controversial aspects of the insider trading directive are its enforcement provisions.⁹⁷ The Directive addresses enforcement on several fronts. The first is the stringency with which each Member State must conform to the various regulations.⁹⁸ According to the Directive, each Member State must adopt national legislation at least as stringent as that provided in the Directive.⁹⁹ A Member State may, however, adopt more stringent provisions, and extend the scope of the Directive to include prohibitions against a tippee trading on insider information.¹⁰⁰

The second major enforcement issue that the Directive addresses is the administration of a Member State's insider trading prohibitions.¹⁰¹ To this end, the Directive simply requires that each Member State designate an administrative authority which will be responsible for ensur-

93. See Fornasier, *supra* note 47, at 165 (stating that the Court requires Member States to strictly conform national legislation with Community law).

94. *Id.*

95. *Id.*

96. See *supra* note 22 and accompanying text (illustrating that only these three Member States have criminal insider trading regulations).

97. See Note, *Toward the Unification*, *supra* note 11, at 449 (stating that the major weakness in the Directive is its enforcement provisions).

98. See *id.* (explaining that one of the basic policy reasons of the Directive is assuring equal protection in each Member State).

99. *Council Directive*, *supra* note 32, art. 6. Article 6 provides in relevant part: "Each Member State may adopt provisions more stringent than those laid down by this Directive or additional provisions, provided that such provisions are applied generally." *Id.*

100. *Id.* Article 6 further provides: "In particular [a Member State] may extend the scope of the prohibition laid down in Article 2 and impose on persons referred to in Article 4 the prohibitions laid down in Article 3." *Id.*

101. See Note, *Toward the Unification*, *supra* note 11, at 449 (recognizing that the Directive fails to establish guidelines to ensure uniform administration).

ing compliance with its insider trading laws.¹⁰² This authority must be given the investigatory and supervisory prerogative to carry out its regulatory purpose.¹⁰³ Furthermore, each country bears the responsibility for informing every Member State which agency will be regulating insider trading, and endowing its regulatory bureau with the power to cooperate with authorities.¹⁰⁴

Inter-EEC cooperation in the regulation of insider trading is the primary function of the Council Directive. This cooperation is, therefore, a critical element in controlling the relatively new phenomenon of transnational insider trading.¹⁰⁵ As a result, each Member State must endow its designated national authority with the power to investigate and manage suspected insider trading violations in cooperation with other national authorities.¹⁰⁶ Several important issues which require careful consideration are apparent. If the exchange of information might compromise the "sovereignty, security, or public policy"¹⁰⁷ of the state receiving a request, for example, then that state's authority may refuse to act on a request.¹⁰⁸ A state's authority may also refuse a request if the party who is the subject of the investigation has previously participated in judicial proceedings on the same action in the state receiving the request.¹⁰⁹ Finally, to facilitate mutual cooperation, a requesting state may forward information it receives to other Member States, if the state that supplied the information consents.¹¹⁰

102. *Council Directive, supra* note 32, art. 8, (1)(2). The Directive provides that:

1. Each Member State shall designate the administrative authority or authorities competent, if necessary in collaboration with other authorities to ensure that the provisions adopted pursuant to this Directive are applied. It shall so inform the Commission which shall transmit that information to all Member States.

2. The competent authorities must be given all supervisory and investigatory powers that are necessary for the exercise of their functions, where appropriate in collaboration with other authorities.

Id.

103. *Id.*

104. *Id.*

105. *See European Community Commission Proposes Ban on Insider Trading*, 19 SEC. REG. L. REP. (BNA) 636 (1987) (stating that the Directive's proposed information exchange system serves an important role in the effort to curb insider trading across the EEC's national borders); *see also* Comment, *New EEC Draft Directive, supra* note 38, at 139 (relating the relevant provisions of the Directive to the cases of insider trading crossing national boundaries).

106. *Council Directive, supra* note 32, art. 10(1). The Directive mandates that present and former enforcement officials maintain professional secrecy when dealing with the transnational exchange of information. *Id.*

107. *Council Directive, supra* note 32, art. 10(2)(a).

108. *Id.*

109. *Id.* at art. 10(2)(b).

110. *Id.* at art. 10(3).

To further enhance cooperation, the Directive provides for the establishment of a "contact committee" at the Community level to function as a working body charged with exchanging information among Member States, and suggesting regulatory changes.¹¹¹ By providing for both the contact committee—a standing committee that has experience working together¹¹²—and the provisions spelled out in Article 8, which will help make the exchange of information less formal,¹¹³ the Directive may achieve the uniform level of regulation that it seeks to create.

In terms of the "external competence" of the Community in dealing with international enforcement of the Directive, Article 11 provides that, "[t]he Community may, in conformity with the Treaty, conclude agreements with non-member countries on the matters governed by this Directive."¹¹⁴ While this statement appears fairly straightforward, some commentators speculate on the legal effect of Article 11 with pessimism.¹¹⁵ They base their reservations on the fact that EEC institutions cannot confer competence on the Community in the field of international law.¹¹⁶ Because the Directive derives its authority from Article 100a of the Treaty of Rome,¹¹⁷ analysts should interpret Article 11 to allow Member States to conclude international agreements on their own, as long as the agreements do not compromise the Directive's provisions or future developments in Community law.¹¹⁸ Although Article 11 may merely represent a policy initiative,¹¹⁹ it illustrates that the EEC is aware of the need for insider trading enforcement on an international level.

111. *Id.* at art. 12. The Council first created contact committees to facilitate implementation of the Directive. Note, *Toward the Unification*, *supra* note 11, at 437 n.32. Representatives of the Commission and other persons appointed by the Member States comprise these committees. *Id.* at 437-38.

112. See Fornasier, *supra* note 47, at 170 (noting that the standing committee members are accustomed to working together).

113. See *id.* at 168-69 (stating that by giving the authorities appointed by the Member States a role that is more administrative than judicial, the provisions promote an informal atmosphere which may create a smooth network of powerful national regulatory authorities).

114. *Council Directive*, *supra* note 32, art. 11.

115. See Fornasier, *supra* note 47, at 174 (speculating that Article 11 is merely a general policy statement with no real legal impact).

116. *Id.* at 171.

117. See Treaty of Rome, *supra* note 34 and accompanying text (discussing the power of the Treaty of Rome).

118. See Fornasier, *supra* note 47, at 172 (concluding that analysts cannot interpret Article 11 to confer competence on the Community in matters of foreign affairs and that individual Member States may conclude international agreements on their own).

119. See *id.* at 174 (asserting that Article 11 may simply be a policy statement devoid of legal significance).

5. Sanctions/Penalties

While the exchange of information and mutual cooperation standards that the Directive envisions represent a substantial step toward uniform regulation of insider trading, the manner in which the Directive approaches the application of sanctions to violators is a source of considerable speculation.¹²⁰ The Directive allows each Member State to determine its own penalties.¹²¹ Many consider this a matter of principle in formulating Community law, as the Commission considers penal sanctions the exclusive domain of each individual Member State.¹²² As a result, however, it is possible that one state would implement both criminal and civil sanctions, while others would choose one of the two penalties.¹²³ This inconsistency between sanctions threatens EEC harmonization.¹²⁴

An analysis of the prospects for the Directive's success or failure should consider past treatment of insider trading in individual Member States. Two Member States (the United Kingdom and Germany) have approached insider trading from substantially different angles. An examination of insider trading regulations in these countries may illustrate the prospects for success on a Community-wide basis for two reasons. First, because the regulatory provisions in the United Kingdom served as a model for the creation of the EEC Directive, those countries which must now implement a regulatory scheme may learn from the various successes and failures of the British system. Second, because Germany does not statutorily regulate insider trading, and because its markets are similar to those of the seven Member States that have not dealt with the problem, Germany's treatment and philosophi-

120. See *id.* at 167 (speculating that the differences in sanctions among Member States may jeopardize the Directive's aim of integrating the national markets).

121. See *Council Directive*, *supra* note 32, art. 13. (providing that "[e]ach Member State shall determine the penalties to be applied for infringement of the measures taken pursuant to this Directive . . . [and] [t]he penalties shall be sufficient to promote compliance with those measures").

122. See *Nieuwdorp*, *supra* note 22, at 42-43 (stating that each Member State exercises control over penal law).

123. See *id.* at 43 (explaining that Member States have a choice of penalties).

124. See *Fornasier*, *supra* note 47, at 167 (stating that while all Member States define insider trading consistently, each state may treat this activity differently in terms of legal qualifications and sanctions); see also *Comment, New EEC Draft Directive*, *supra* note 38, at 139 (asserting that the Directive will not achieve harmonization until it consistently applies sanctions throughout the Community). *But see Fornasier*, *supra* note 47, at 167 (noting that Article 13 does provide that sanctions must be stiff enough to force compliance, and that the Commission as well as the Court of Justice may review a state's penal provisions and bring them into conformity with the Directive's aims).

cal approach to insider trading may influence the way that many of the Member States treat the new Directive.

III. THE REGULATION OF INSIDER TRADING IN GREAT BRITAIN

A. HISTORICAL TREATMENT

The United Kingdom has faced the insider trading issue since the early 20th century.¹²⁵ Because the United Kingdom is a common law state, the British courts promulgate regulations. In the landmark case of *Percival v. Wright*,¹²⁶ the United Kingdom's Court of Chancery addressed the fiduciary relationship that exists among the corporation's directors, the corporate entity, and its shareholders. The court held that while corporate directors do have a fiduciary relationship with the corporate entity, they do not have such a relationship with its shareholders.¹²⁷ Therefore, investors may not bring an insider trading claim against a company's directors.¹²⁸ While *Percival* did establish the right of a corporation to sue its directors, very few corporations have taken advantage of this due to their reluctance to sue colleagues.¹²⁹ While some investors have attempted to redress their grievances through alternative causes of action, such as breach of confidence, duty to disclose, and unjust enrichment, the courts have applied these theories narrowly, and most plaintiffs have had little success in attaining adequate remedies.¹³⁰

The United Kingdom also utilizes a self-regulatory approach to insider trading. London's financial center, "the City," is comprised of a closely knit group which has traditionally governed its own activities.¹³¹ The custom of self-regulation stems from the fear that if unabated insider trading occurs, the government will impose regulatory measures against the practice.¹³² Two United Kingdom institutions have tradi-

125. See *Percival v. Wright*, 2 Ch. 421, 426-27 (1902) (dismissing an action against a corporation's directors accused of insider trading).

126. *Id.*

127. *Id.* at 425-26.

128. *Id.*

129. See Rider, *supra* note 55, at 155 (stating that often the insider is an upper-level manager or director, and his associates are reluctant to sue).

130. See *id.* at 158-60 (discussing judicial solutions to insider trading claims and their ultimate failure).

131. See Comment, *Recent Developments in Insider Trading Laws and Problems of Enforcement in Great Britain*, 12 B.C. INT'L & COMP. L.R. 265, 268 (1989) [hereinafter Comment, *Recent Developments*] (stating that the City has historically regulated itself absent significant government intervention).

132. Rider, *supra* note 55, at 160.

tionally regulated insider trading, the City Panel on Takeovers and Mergers¹³³ and the Council for the Securities Industry.¹³⁴

The City Panel promulgates a professional code of regulations regarding commercial conduct during takeovers and mergers—the City Code.¹³⁵ The Code applies to any company listed on the stock exchange.¹³⁶ It prohibits employees who have “confidential price sensitive information,” and who work for a company engaged in a merger or takeover, except the offeror, from dealing in the stock of the companies involved.¹³⁷ The Code also prevents employees under its prohibitions from counseling or advising a third party with respect to purchasing the target securities.¹³⁸ While the City Panel can regulate insider trading during takeovers and mergers through the City Code, it cannot address the issue in other contexts.¹³⁹ Whereas the City Panel issues and enforces regulations, the Council for the Securities Industry’s primary function is to examine and recommend solutions to insider trading problems.¹⁴⁰

Although there has been significant statutory regulation of insider trading over the last ten years, both the City Panel and the Council of Securities Industry continue to operate in a watchdog capacity.¹⁴¹ In order to assist the City’s self-regulatory measures,¹⁴² Parliament, in 1980, made insider trading a statutory violation in the United King-

133. Comment, *Recent Developments*, *supra* note 131, at 270. The United Kingdom’s financial services industry established the City Panel on Takeovers and Mergers in 1968, following almost two decades of insider trading abuse. *Id.* Representatives from the financial services industry, including members of the Council of the Stock Exchange, the Exchange’s governing body, as well as bankers, stock brokers, and insurance professionals compose the panel. *Id.* See generally Rider, *supra* note 55, at 160-61 (discussing the City Panel and its development).

134. Wallace, *Who is Subject to the Prohibition Against Insider Trading: A Comparative Study of American, British, and French Law*, 15 Sw. U.L. REV. 217, 235 (1985). Financial services industry professionals compose the Council for the Securities Industry, established in 1978. *Id.*

135. A. JOHNSON, CITY CODE ON TAKE-OVERS AND MERGERS 158-59 (1980).

136. See Comment, *New EEC Draft Directive*, *supra* note 38, at 124 (stating that a company is not bound by the Code unless it wishes to trade on the national stock exchange).

137. See Comment, *Recent Developments*, *supra* note 131, at 270 (discussing the City Code’s prohibitions).

138. *Id.*

139. *Id.* at 271.

140. See Wallace, *supra* note 134, at 235 (discussing the role of the Council for the Securities Industry).

141. See Comment, *New EEC Draft Directive*, *supra* note 38, at 124 (stating that statutory regulation has amplified the role these institutions play in securities regulation).

142. See *id.* (explaining that the United Kingdom promoted statutory regulation, not because self-regulation failed, but rather to reinforce self-regulation by providing harsher sanctions).

dom.¹⁴³ Parliament consolidated the insider trading provisions of the Companies Act of 1980, combined them with other company law regulations,¹⁴⁴ and in 1985 adopted the Company Securities Insider Dealing Act (Insider Act).¹⁴⁵ By providing for criminal sanctions against persons convicted of insider trading, the Insider Act strengthened the regulatory authorities' powers.¹⁴⁶ In 1986, Parliament passed the Financial Services Act (Financial Act),¹⁴⁷ again increasing the investigatory powers of securities regulators.¹⁴⁸ Importantly, the Financial Services Act added civil penalties to the list of available insider trading sanctions.¹⁴⁹ Notwithstanding the additional insider trading provisions of the Financial Services Act, the Insider Act serves as the principal law regulating insider trading in the United Kingdom.¹⁵⁰

B. DEFINITIONS AND SCOPE OF THE INSIDER ACT

As in the EEC Council Directive, the definitions of "inside information" and "insider" provide significant insight into the scope of the British insider trading regulations. Three important elements exist in the definition of inside information in the Insider Act.¹⁵¹ First, the Act prohibits an insider from dealing securities on a recognized stock exchange if the person obtains information through a connection with a

143. Companies Act, 1980, ch. 22.

144. See Comment, *Recent Developments*, *supra* note 131, at 276 (discussing the enactment of the 1985 Insider Act); see also Banoff, *The Regulation of Insider Trading in the United States, United Kingdom, and Japan*, 9 MICH. Y.B. INT'L LEGAL STUD. 145, 154 (1987) (discussing the re-enactment of the 1980 Companies Act as the 1985 Insider Act).

145. Company Securities Insider Dealing Act, 1985, ch. 8 [hereinafter Insider Act].

146. See Note, *Toward the Unification*, *supra* note 11, at 438-39 (discussing the impact of the Insider Act on regulatory authorities).

147. Financial Services Act, 1986, ch. 60 [hereinafter Financial Act].

148. *Id.* at § 173-78.

149. *Id.* at § 62.

150. See Houle, *Survey of National Legislation Regulating Insider Trading*, 9 MICH. Y.B. INT'L LEGAL STUD. 209, 211 (1987) (noting the importance of the Insider Act in addressing the United Kingdom's insider trading problem).

151. Insider Act, *supra* note 145, at § 10. The Insider Act defines inside information as:

Any reference in this Act to unpublished price-sensitive information in relation to any securities of a company is a reference to information which—

(a) relates to specific matters relating or of concern (directly or indirectly) to that company, that is to say, is not of a general nature relating or of concern to that company, and

(b) is not generally known to those persons who are accustomed or would be likely to deal in those securities but which would if it were generally known to them be likely materially to affect the price of those securities.

Id.

corporation that would otherwise be unavailable to persons dealing in securities.¹⁵² Second, the information regarding a particular company or security must be specific in nature.¹⁵³ Finally, the information must be likely to materially affect the price of the security if the corporation published the information.¹⁵⁴

The Insider Act employs a broad definition of "insider" that includes "primary" and "secondary" insiders.¹⁵⁵ The Act has a wide scope and is the most inclusive insider trading legislation in Europe.¹⁵⁶ The heart of the insider prohibitions can be found in Section (1) of the Act—its statutory definition of insider.¹⁵⁷ A primary insider under the Act's definition is a fiduciary of the entity issuing the target security.¹⁵⁸ The "insider" must be "knowingly connected" with the issuer or associated with the company during the prior six months.¹⁵⁹ "Connected" persons include all directors, and other persons who occupy a position reasonably expected to provide access to the privileged information and reasonably expected not to disclose such information, unless acting within their scope of employment.¹⁶⁰ The Act also covers temporary insiders, a

152. *Id.* at § 10(b). Note that the extent to which the information is unavailable to people dealing in the market is uncertain. Banoff, *supra* note 144, at 156. It does not appear that the information has to be available to the general public. *Id.*

153. Insider Act, *supra* note 145, at § 10(a). The meaning of the word specific is an unresolved issue. At least one commentator defines it to include mergers, acquisitions, major business decisions, dividend payments, changes in capital structure or investment, and divestitures. Banoff, *supra* note 144, at 157 (citing J.H. FARRAR, COMPANY LAW 356 (1985)).

154. Insider Act, *supra* note 145, at § 10(b). The information must be likely to affect the actual price of the security, not just play an important role in the trading decisions of third parties. Banoff, *supra* note 144, at 156.

155. See Insider Act, *supra* note 145, at § 1 (1) - (4) (prohibiting different types of conduct for different categories of insiders).

156. See *Harmonization of the Member States*, *supra* note 78, at 169 (discussing the scope of the Insider Act).

157. Insider Act, *supra* note 145, at § 1. The Insider Act provides in full:

(1) Subject to section 3, an individual who is or at any time in the preceding 6 months has been, knowingly connected with a company shall not deal on a recognized stock exchange in securities of that company if he has information which—

(a) he holds by virtue of being connected with the company,

(b) it would be reasonable to expect a person so connected, and in the position by virtue of which he is so connected, not to disclose except for the proper performance of the functions attaching to that position, and

(c) he knows is unpublished price-sensitive information in relation to those securities.

Id.

158. See Banoff, *supra* note 144, at 141 (stating that "all insiders are fiduciaries, but not all fiduciaries are insiders").

159. Insider Act, *supra* note 145, § 1(1).

160. Banoff, *supra* note 144, at 155. The definition of a "connected" person includes those employees who have access to inside information and who would be ex-

second group of primary insiders who are not permanent employees of the company.¹⁶¹

A major difference between the Insider Act and the EEC Directive is that the British Act covers individuals, not corporations.¹⁶² The United Kingdom will, therefore, have to amend its laws in order to bring them into conformity with the Directive. This should not pose a significant problem, however, for as the Insider Act illustrates, the United Kingdom already embraces a broad definition of "insider."¹⁶³

The second major group of people covered under the Insider Act are secondary insiders, or tippees.¹⁶⁴ A tippee is generally defined as one who "knowingly"¹⁶⁵ receives his insider information from a "connected" person.¹⁶⁶ The inclusion of secondary insiders in the insider trading prohibitions makes the British Act the broadest European insider trading law.¹⁶⁷

One major caveat in the insider definition is its scienter requirement.¹⁶⁸ As the Act contains criminal provisions, there is a mens rea element.¹⁶⁹ To sustain a conviction for insider trading, the Act requires the suspected insider to be *knowingly* connected with the corporate en-

pected not to reveal that information except when acting within the scope of their employment. *Id.*

161. Insider Act, *supra* note 145, § 9. A temporary insider engages in a professional relationship with the issuer, or the companies that have such a relationship employ temporary insiders. Banoff, *supra* note 144, at 155. As with the insider, this type of fiduciary reasonably is expected to be privy to the inside information and not disclose it, except in the performance of his or her duties. *Id.* This type of insider includes lawyers, accountants, auditors, or stock brokers. Comment, *Recent Developments*, *supra* note 131, at 277.

162. See Banoff, *supra* note 144, at 155 (stating that while the Act does not expressly cover corporations, authorities may regard them as aiders and abettors).

163. *Id.*

164. See Insider Act, *supra* note 145, § 1(3) - (4) (prohibiting certain types of conduct).

165. Banoff, *supra* note 144, at 156. An important aspect of this provision deals with the term knowingly. *Id.* There must be specific knowledge about the security being issued. *Id.* Thus, a tipper's mere advice to trade, without more specificity, does not fall under the Act. *Id.*

166. *Id.* Under this portion of the Act, a connected person is one whom the tippee has reason to believe received the information due to his position; reasonably expected that one in the tipper's position would not disclose the information; and has good cause to believe that the information is "price sensitive." *Id.*

167. See Comment, *Harmonization of the Member States*, *supra* note 78, at 170 (stating that by including tippees, the British insider laws are more inclusive than the West German or the French laws); see also Cruickshank, *supra* note 1, at 346-47 (commenting that the United Kingdom Insider Act, by including tippees, is the broadest in Europe).

168. Insider Act, *supra* note 145, § 1(1) - (3).

169. Comment, *New EEC Draft Directive*, *supra* note 38, at 126. One can infer the mens rea requirement from section 3 of the Insider Act. It provides a defense to insider trading if there is a lack of profit motive. *Id.*

tity,¹⁷⁰ to *know* that the insider obtained privileged information through that position, and to *know* that the information was price-sensitive and non-public.¹⁷¹ This position focuses on secondary insiders, as the Act will not render them liable unless they knew that an insider disclosed the information, *and* that the information was privileged.¹⁷²

Having set forth the critical definitional elements of the Insider Act, an analysis of what actions are prohibited under the Act as compared to the EEC Directive is useful. The British Insider Act prohibits a broader range of activities than does the EEC.¹⁷³ The Directive only prohibits trading based on the acquisition of inside information.¹⁷⁴ The British Act, however, prohibits a number of activities, including trading,¹⁷⁵ tipping,¹⁷⁶ and counseling or procuring.¹⁷⁷ One can be guilty under the law if he or she tips someone who in turn takes no action with regard to the target security.¹⁷⁸ Another significant difference between the Insider Act and the Directive is that one who is in possession of privileged information may not counsel or procure a tippee if he or she reasonably believes that the tippee will take advantage of the information outside of Great Britain.¹⁷⁹ These differences are crucial. In examining the effectiveness of the EEC Directive, at least with respect to

170. See Banoff, *supra* note 144, at 158 (stating that one aspect of the scienter requirement is knowledge of the corporate connection).

171. *Id.*

172. See Comment, *New EEC Draft Directive*, *supra* note 38, at 126 (stating that the scienter requirement applies to both primary and secondary insiders and requires knowledge of insider and inside information status).

173. See *infra* notes 174-81 and accompanying text (comparing the breadth of the EEC regulations to the breadth of the Insider Act).

174. *Council Directive*, *supra* note 32, art. 2. Article 2 of the Directive prohibits an insider from "acquiring" or "disposing" of transferable securities for his, or a third party's advantage; through, for example, trading. *Id.* The statute, however, does not expressly prohibit any other action. *Id.*

175. Insider Act, *supra* note 145, at § 1.

176. *Id.* at § 1 (7)-(8). This prohibition essentially prevents a tipper or tippee from advising someone else to trade if the advisor has reason to believe that the advisee will either trade or tip again. Banoff, *supra* note 144, at 158.

177. Insider Act, *supra* note 145, at § 1(7). The counseling and procuring prohibition is another example of the ways in which United Kingdom insider laws reach a greater number of potential offenders than the EEC Directive. Counseling and procuring is like tipping, except that the parties exchange no specific information. Banoff, *supra* note 144, at 158. A tippee is liable under the Act, but a counselee is not. *Id.* Finally, a counselor, in addition to a tipper, is liable under the Act. Insider Act, *supra* note 145, at § 1.

178. See Banoff, *supra* note 144, at 158 (stating that it is a crime for a non-dealing tipper to disclose inside information to a non-dealing tippee).

179. Insider Act, *supra* note 145, at § 5. Note that section 5 simply takes those acts prohibited under sections 1 and 2, and applies them to extra-territorial situations. Houle, *supra* note 150, at 213. Note that as in sections 1 and 2, the Act also prohibits one from tipping, counseling, or procuring another who is outside Great Britain. *Id.*

the United Kingdom, it is clear that the prohibitions spelled out by the EEC compliment the existing system in Great Britain because the scope of the United Kingdom prohibitions is much more comprehensive.¹⁸⁰

C. DEFENSES

While the statutory prohibitions included in the Insider Act are more stringent than the EEC Directive, the British insider regulations differ from the EEC Directive in a significant and potentially troublesome way. The United Kingdom's Insider Act provides six defenses to an accusation of insider trading,¹⁸¹ while the Directive provides no defenses.¹⁸² The Insider Act divides defenses into two groups—individual actions that are not prohibited, and actions that are not prohibited if the individual acquires information in a particular manner.¹⁸³

The first group of defenses applies to persons trading or counseling for purposes other than making a profit or avoiding a loss,¹⁸⁴ or trading in good-faith according to fiduciary requirements.¹⁸⁵ The second group is available to professionals who deal on a recognized stock exchange, acquire their information in the regular course of business, and trade or counsel in the good-faith practice of their profession.¹⁸⁶ Because of these defenses, it is apparent that Great Britain and the EEC are inconsistent in determining permissible use of privileged information.

180. See *supra* note 167 (discussing the inclusiveness of the British Insider Act).

181. See Insider Act, *supra* note 145, at § 3 (providing six exceptions to the insider trading provisions).

182. Council Directive, *supra* note 32.

183. See Insider Act, *supra* note 145, at § 3 (dividing the defense offered into two sections).

184. Insider Act, *supra* note 145, at § 3 (1). Section 3(1) provides that "(1) Sections 1 and 2 do not prohibit an individual by reason of his having any information from—(a) doing any particular thing otherwise than with a view to the making of a profit or the avoidance of a loss (whether for himself or another person) by the use of that information." *Id.* at § 3(1)(a). See Comment, *Harmonization of the Member States*, *supra* note 78, at 175 (comparing this provision to the lack of provisions in France and the United States); Comment, *Recent Developments*, *supra* note 131, at 279 (describing these traders as persons exempt from the Insider Act's prohibitions).

185. Insider Act, *supra* note 145, at § 3(1)(b). Section 3 provides that "Sections 1 and 2 do not prohibit an individual by reason of his having any information from—(b) entering into a transaction in the course of the exercise in good faith of his functions as liquidator, receiver or trustee in bankruptcy. . . ." *Id.*

186. Insider Act, *supra* note 145, at § 3(1)(c). Section 3 of the Insider Act provides in relevant part:

Sections 1 and 2 do not prohibit an individual by reason of his having any information from—

(c) doing any particular thing if the information—

(i) was obtained by him in the course of a business of a jobber in which he was engaged or employed, and

Consequently, this may frustrate harmonization of Member State laws with the EEC Directive.

D. ENFORCEMENT

"It has been repeatedly emphasi[z]ed that the Achilles heel of insider trading regulations, not only in Britain but in other jurisdictions as well, is inadequate enforcement."¹⁸⁷ In response to historically inadequate enforcement of Great Britain's insider trading laws,¹⁸⁸ Parliament passed the Financial Services Act of 1986.¹⁸⁹ Most significantly, the Financial Act increases investigatory powers for the discovery of insider trading.¹⁹⁰ Parliament allocated investigatory powers to the Department of Trade and Industry (DTI),¹⁹¹ Great Britain's primary securities enforcement agency. According to the Financial Act, if the Secretary of State suspects an Insider Act violation, the Secretary may designate DTI employees to investigate the purported violation.¹⁹²

The Financial Act grants the appointed investigators with a broad range of powers,¹⁹³ including the ability to demand relevant docu-

(ii) was of a description which it would be reasonable to expect him to obtain in the ordinary course of that business, and he does that thing in good faith in the course of that business.

"Jobber" means an individual, partnership or company dealing in securities on a recognized stock exchange and recognized by the Council of the Stock Exchange as carrying on the business of a jobber.

Id.

The Act does not prohibit a jobber from dealing or taking any other actions with regard to a particular security if he does it in order to facilitate the completion of a transaction that was already in progress when the jobber obtained privileged information. *Id.* at § 3(2); *see also* Comment, *Recent Developments*, *supra* note 131, at 279-80 (stating that a person can defend an insider trading charge by asserting that he or she traded on privileged information in order to carry out a transaction).

187. P. Tridimas, *The Financial Services Act and the Detection of Insider Trading*, 8 COMPANY LAW. 162, 164 (1987).

188. *See id.* at 164 (stating that between 1980 and 1987 only seven out of the more than 100 cases referred by the Stock Exchange to the Department of Trade and Industry led to prosecutions).

189. Financial Act, *supra* note 147; *see* Banoff, *supra* note 144, at 162 (discussing new powers afforded to the Securities Industry Board by the Financial Securities Act).

190. *See* Tridimas, *supra* note 187, at 162 (stating that the most important aspect of the Act, in terms of insider trading, is the new special investigatory power it created); *see also* Banoff, *supra* note 144, at 161 (commenting on how the Financial Services Act increased the enforcement powers of the Department of Trade and Industry).

191. *See* Banoff, *supra* note 144, at 161 (discussing the enforcement powers of the DTI).

192. Financial Act, *supra* note 147, at § 177(1).

193. *See* Tridimas, *supra* note 187, at 161-62 (discussing some of the investigatory provisions of the Act).

ments,¹⁹⁴ to force "all assistance" in furthering an investigation,¹⁹⁵ and to examine persons under oath.¹⁹⁶ Finally, to add substance to the new provisions, the Financial Act provides for the imposition of sanctions on a non-cooperative party.¹⁹⁷ After the DTI investigates a suspected insider and concludes that a violation has occurred, it refers the case to the secretary of state.¹⁹⁸ The secretary of state may then either bring charges or refer the matter to the director of public prosecutions who may begin criminal proceedings.¹⁹⁹ The Financial Act's enforcement system complies with Article 8 of the Council Directive, which requires that each Member State designate a competent authority to ensure adequate enforcement of the state's insider laws.²⁰⁰

E. SANCTIONS AND PENALTIES

The sanctions available to deter financial misconduct are the final element to consider in examining the British enforcement provisions. Because of the difficulty in identifying injured parties in an insider trading action, the Insider Act provides only for criminal penalties.²⁰¹ A convicted insider may face up to two years imprisonment, or a fine of an unspecified amount.²⁰² Although the Insider Act does not provide for civil remedies, the Financial Act provides an opportunity for civil

194. Financial Act, *supra* note 147, at § 177(3). When seeking information from bankers, the investigators must believe that the customer will be able to give specific information regarding a suspected violation, and the information must convince the Secretary of State that disclosure is necessary. *Id.* at § 177(8).

195. *Id.* at § 177(3)(c).

196. *Id.* at § 177(4). Under the Act investigators may use any statement made during the investigation against the person who is complying with the Act. *Id.* at § 177(6).

197. *Id.* at § 178(2). Section 178 of the Act authorizes punishment of a person as if he was in contempt of court. *Id.* at § 178(2)(a). The secretary of state can impose severe penalties on a non-cooperative party. *Id.* at § 178(2)(b). These sanctions severely restrict a recalcitrant subject's ability to work in the financial services industry. *Id.* § 178(3).

198. Insider Act, *supra* note 145, at § 8(2).

199. *Id.*

200. See Council Directive, *supra* note 32, art. 8 (declaring that authorities competent to enforce the insider trading provisions must be given all supervisory and investigative powers necessary for enforcement).

201. See Comment, *Recent Developments*, *supra* note 131, at 290-91 (stating that because there are no civil penalties under the Insider Act, an insider is able to keep his or her profits even if convicted); Houle, *supra* note 150, at 213 (stating that the Insider Act provides no civil penalties); see also Banoff, *supra* note 144, at 162 (stating that the Insider Act does not contain any civil penalties, but that there are possible civil remedies under the Financial Services Act).

202. Insider Act, *supra* note 145, at § 8(a). In Great Britain there is a summary judgment conviction system; an insider convicted under this scheme faces a maximum penalty of six months imprisonment, a fine, or both. *Id.* at § 8(b).

actions.²⁰³ The Securities Industry Board (SIB) suggests that it has new-found power to seek injunctive relief or force disgorgement through restitution proceedings under the Financial Act.²⁰⁴ Some commentators, however, suggest that greater civil measures are necessary in order to effectively combat insider trading.²⁰⁵ Specifically, effective enforcement requires express civil remedies that are not subject to court interpretation.²⁰⁶ One commentator suggests that the British government pass laws enabling the DTI, the SIB, or the company whose shares were traded illegally, to sue the insider directly in order to recover illegally gained profits.²⁰⁷ In support of this position, this commentator points to the effectiveness of civil relief in the United States provided by the Securities Exchange Act of 1934.²⁰⁸

Although the British provisions appear to be in compliance with the goals and regulations of the Council Directive, it is unclear how effective they will be in light of past enforcement records. For example, from 1980-1987 the DTI investigated over one hundred cases referred by the stock exchange.²⁰⁹ Only ten prosecutions and seven convictions

203. See Note, *Toward the Unification*, *supra* note 11, at 440 (stating that the Financial Act creates new possibilities for investors wishing to sue for damages); N. POSER, *INTERNATIONAL SECURITIES REGULATION* § 3.4.5, at 178-79 (1991) [hereinafter Poser] (explaining various ways in which a private investor may bring a civil lawsuit under the Financial Services Act and new rules promulgated by the SIB).

204. See Banoff, *supra* note 144, at 162 (noting that the SIB has suggested that it has new powers under the Financial Services Act); Poser, *supra* note 203, § 3.7.4, at 290-92 (describing the SIB's powers to seek injunctions and restitution orders).

205. See Comment, *Recent Developments*, *supra* note 131, at 297 (stating that a lack of civil remedies in the United Kingdom is an obstacle to effective insider trading enforcement); *but see* Poser, *supra* note 203, § 3.7.6, at 293-98 (discussing the implications of section 62 of the Financial Services Act which provides for private lawsuits and imposes liabilities on issuers and other fiduciaries).

206. Comment, *Recent Developments*, *supra* note 131, at 298. Parliament needs to provide express remedies because the courts have not applied basic common law principles to insider trading cases. *Id.* Parliament has not given the courts incentive to broaden the scope of the common law in this area; the Insider Act expressly states that no transaction is void *per se* as a result of violations of the Act's provisions. See Insider Act, *supra* note 145, at § 8(3) (excepting transgressions of certain provisions of the Act from grounds for voidability). In addition, the British government opposes using civil remedies against insiders due to a perception of impracticality. Comment, *Recent Developments*, *supra* note 131, at 297-98.

207. See Comment, *Recent Developments*, *supra* note 131, at 298 (advocating the use of certain civil remedies).

208. *Id.* at 290. Section 16(b) of the Securities Exchange Act of 1934 provides civil restitution for corporations and shareholders. *Id.* Courts also have implied a cause of action for injured investors from section 10(b) of the 1934 Act and Rule 10b-5, a regulation promulgated under the Act. *Id.* Many view these remedies as positive measures that encourage investors and companies to bring suits against suspected violators. *Id.*

209. *Id.* at 295. See generally, L. LOSS, *FUNDAMENTALS OF SECURITIES REGULATION* 723-810 (1988) (providing a comprehensive discussion of Rule 10b-5).

resulted from these referrals.²¹⁰ This demonstrates that enactment of legislation may not change a nation's approach to a particular issue. It may be easy to harmonize the EEC's laws, but it will be far more difficult to harmonize its Member States' hearts.

IV. THE REGULATION OF INSIDER TRADING IN THE FEDERAL REPUBLIC OF GERMANY

A. HISTORICAL APPROACH

While the United Kingdom has a fairly rigorous scheme of statutory insider trading prohibitions, the Federal Republic of Germany has only voluntary guidelines.²¹¹ Historically, no tradition of insider trading regulation in either the German corporation (company) or stock exchange law existed.²¹² In the 1960's, however, some investors, wary of stock market abuses, began advocating for a stock exchange law prohibiting insider trading.²¹³ As a result, in November 1970, a committee of stock exchange experts,²¹⁴ established by the Ministry of Economics, adopted the Recommendations for the Solution of the So-Called Insider Problems, a voluntary code.²¹⁵ The Federal Republic of Germany and Great Britain's divergent approach to insider trading and the central role that Germany plays in European economics indicate that an analysis of Germany's experience regulating insider trading is useful in de-

210. *Id.* It also should be noted that by 1987 no one convicted of violating the insider provisions had gone to prison, and the overall sentencing was rather light. Houle, *supra* note 150, at 163.

211. See Houle, *supra* note 150, at 218 (noting that insider regulations in West Germany are not part of federal law, but only serve as guidelines which operate on a contractual level between employees and employers); see also Note, *Toward the Unification*, *supra* note 11, at 442 (stating that Germany's insider guidelines are voluntary); Rider, *supra* note 55, at 245 (stating that the goal of the insider provisions was to encourage voluntary self-regulation).

212. Hopt, *The German Insider Trading Guidelines—Spring-gun or Scarecrow?*, 8 J. COMP. BUS. & CAPITAL MKT. L. 381 (1986).

213. See *id.* (noting that investors had become increasingly reluctant to participate in the market as a result of the large losses suffered by uninformed investors). The German government supported an examination of the securities market due to the suspected significant abuse by insiders. Rider, *supra* note 55, at 245.

214. See Rider, *supra* note 55, at 245 (stating that the Federal Minister of Economic Affairs formed the committee in 1968 to make recommendations for amending German securities laws). It was composed of all parties who the regulations would affect. Houle, *supra* note 150, at 218. Its goal was to reform the stock markets in order to encourage investment. J. Zahn, *Regulation of Insider Trading in the Federal Republic of Germany*, 2 INT'L BUS. L. 92 (1974).

215. See Zahn, *supra* note 214, at 92 (stating that the committee ratified the voluntary code unanimously); Rider, *supra* note 55, at 245 (discussing the approval of the Committee's "Recommendations for the So-Called Insider Problems").

termining the prospects for effective implementation of the Council Directive.

The history of insider trading regulation that preceded the adoption of the voluntary guidelines is sparse. In German company law, the sole provision that even tangentially prohibits insider trading is in the German Act on Stock Corporations.²¹⁶ This Act imposes a standard of care²¹⁷ upon the members of the Vorstand.²¹⁸ Because directors have a responsibility to ensure that a company uses its holdings for the good of the business, the law could apply to insider trading cases.²¹⁹

The German courts also have provided some basis for insider regulation.²²⁰ Courts have held that directors must act with "good faith" toward their corporate entity.²²¹ Other decisions require shareholders to exercise "good faith" in dealing with corporate securities and hold company directors liable for the abuse of privileged information.²²² Few regulatory provisions or enforcement powers existed in West Germany at the time the Minister of Economics formed the special committee to examine securities law.²²³

On November 13, 1970, a unanimous²²⁴ Committee²²⁵ passed the Recommendations for the Solution of the So-Called Insider Trading

216. The German Act on Stock Corporations (Aktengesetz) (Sept. 6, 1965, as amended) [hereinafter Stock Act].

217. *Id.* at art. 93 ¶ (I) (as translated in Rider, *supra* note 56, at 243). The Stock Act, *supra* note 216, provides in relevant part:

In managing the company, the members of the Vorstand shall act with the care of a diligent and prudent executive. They shall not reveal any confidential information and secrets of the company, and in particular business and trade secrets, which have become known to them in connection with their activities as members of the Vorstand.

Id.

218. See DICTIONARY OF LEGAL, COMMERCIAL AND POLITICAL TERMS (1986) (defining Vorstand as a "broad management or board of directors of a company").

219. See Rider, *supra* note 55, at 243 (discussing duties and potential liability of corporate managers); see also *id.* at 243-44 (discussing other possible interpretations of German company law that may apply to insider trading).

220. See *id.* at 244 (stating that courts may use German "common law" in some insider trading cases).

221. *Id.*

222. *Id.* There are no cases directly on point regarding management or shareholder duties or obligations under German law. *Id.* The various duties implied from the existing case law are merely speculative of what courts might actually hold if they addressed the issue directly. *Id.*

223. See Blum, *The Regulation of Insider Trading in Germany: Who's Afraid of Self-Restraint?*, 7 NW. J. INT'L L. & BUS. 507, 519 (1986) (commenting that the lack of civil and common law remedies for insider abuse created the need for the guidelines).

224. Zahn, *supra* note 214, at 92.

225. See *supra* note 214 and accompanying text (discussing the formation, composition and function of the Committee of Experts).

Problems. The Committee sought to curb the growing tide of suspected insider abuse²²⁶ in a self-regulating²²⁷ manner and on a voluntary basis.²²⁸ In 1976, upon the recommendation of the Ministry of Finance and the Committee of Stock Exchanges,²²⁹ the Committee replaced the 1970 provisions with the Guidelines of 1976.²³⁰ Many of West Germany's financial services industries assisted in drafting the 1976 rules.²³¹ The new provisions greatly enhanced the original regulations²³² and maintained the support of Germany's major financial institutions.²³³

B. THE LEGAL NATURE OF THE GUIDELINES

Before considering the various provisions of the Guidelines, it is necessary to discuss their legal nature. Contrary to the requirements of the EEC Directive and unlike the Insider Act in the United Kingdom, the German Guidelines are not national law.²³⁴ Companies enter into or

226. See *supra* note 213 and accompanying text (discussing the realization by both investors and the German government of the increased exploitation of the markets through insider trading).

227. See Hopt, *supra* note 212, at 382 (stating that the Committee quickly adopted the self-regulatory guidelines to avert more restrictive legislation).

228. See Zahn, *supra* note 214, at 92 (stating that the goal of the Guidelines is to prevent insider trading through voluntary regulations, and that because the industry considers the provisions to be commercial guidelines there is a willingness to adhere to them); Rider, *supra* note 55, at 245 (stating that the preface to the Committee report on insider trading clearly stated that parties should follow the rules created on a voluntary basis).

229. See Rider, *supra* note 55, at 245 (discussing the roles of the Ministry of Finance and the Committee of Stock Exchanges).

230. *Id.*; see also Hopt, *supra* note 212, at 392 (stating that by 1978, 226 businesses, representing 84% of share capital, recognized the 1976 rules).

231. Rider, *supra* note 55, at 245. The industries that participated in creating the 1976 Guidelines were: the Federation of German Banks, the Federation of German Stock Exchanges, the Federation of General Banks, the Federation of German Industry, the Federation of Federated Business Banks, the Federation of German National Banks and Natural Resource Banks, the Federation of German Retailers, the Federation of German Wholesalers and German Import and Export Merchants, the Federation of the Insurance Companies, and German Savings Banks. *Id.*

232. See Hopt, *supra* note 212, at 391 (commenting that some viewed the initial guidelines as too narrow, and the Committee subsequently broadened them in 1976); see also Rider, *supra* note 55, at 245 (stating that the 1976 provisions made the former guidelines "more rational, practical and flexible").

233. See Hopt, *supra* note 212, at 382 (stating that the Committee has barely reformed the Guidelines since the mid-1970's, and that German financial institutions continue to be the primary supporters of the insider rules).

234. See *supra* note 211 and accompanying text (describing the voluntary nature of the Guidelines); see also Hopt, *supra* note 212, at 383 (stating that the Guidelines are not rules of the state and cannot be accorded semi-mandatory status as trade usages).

opt out of the Guidelines on a strictly private basis.²³⁵ The Guidelines are usually included in the employment contract.²³⁶ Consequently, while various review boards may determine whether a violation has occurred, they have no power to levy sanctions against a disclosed insider.²³⁷ Thus, a company must pursue any litigation on its own.²³⁸

C. DEFINITIONS AND SCOPE OF THE GUIDELINES

The definition of inside information under the German law is broad.²³⁹ The Guidelines define inside information as information concerning known or unknown events which may influence the evaluation of insider records.²⁴⁰ The Guidelines, however, limit the breadth of this statement by listing specific examples of inside information.²⁴¹ This privileged information includes knowledge of substantial changes in corporate earnings, capital, planned dividends, transfers, mergers, acquisitions, and other significant financial considerations.²⁴² Finally, further complicating matters, the uniformly accepted definition of inside

235. See Rider, *supra* note 55, at 246 (noting that *Insider Trading Guidelines* Rules 4 and 5 clearly provide for a solely contractual relationship). Rule 4 states that the Guidelines are strictly voluntary and that violations do not result in criminal or legal proceedings against the violator. *Id.* Rule 5 enforces the contractual nature of the provisions by stating that companies need only request or require that employees adhere to them, and that a violation can lead to an action in contract. *Id.*

236. Hopt, *supra* note 212, at 383. The Guidelines usually apply to management and provide for acceptance of the insider prohibitions. *Id.*

237. *Id.* German law considers a review board to be a vehicle through which an insider and his company conduct arbitration. *Id.*

238. See Rider, *supra* note 55, at 246 (commenting that Rule 4 of the *Insider Guidelines* provides companies a private right of action). Profits that insider trading generates usually revert to the company whose information is disclosed. *Id.*

239. See Hopt, *supra* note 212, at 384 (stating that initially the definition of inside information under the Guidelines appears broad).

240. Rider, *supra* note 55, at 245 (citing *Insider Trading Guidelines*, § 2(3)(1)).

241. See Hopt, *supra* note 212, at 384 (noting that the Guidelines include both a broad prohibition and a specific list of inside information); see also Rider, *supra* note 55, at 245-46 (observing that the definition of inside information includes both general information about a company's financial circumstances and a specific list of prohibitions).

242. Rider, *supra* note 55, at 246 (citing *Insider Trading Guidelines*, § 2(3)(1)). The *Insider Trading Guidelines* provide in relevant part that knowledge of the following constitutes inside information:

- (a) Capital reduction or the raising of capital, including capital increases out of company sources.
- (b) The completion of a management or profit-sharing agreement.
- (c) Takeover or compensation offer.
- (d) Merger, amalgamation, state transferral or modification.
- (e) Liquidation.

Id.

information hinges on whether the information is available to the public and not on whether the inside information is privileged.²⁴³

Since differing interpretations of the definition in the guidelines could confuse its meaning and broaden its scope, a more general definition could resist uncertainty.²⁴⁴ Such a definition might include prohibitions on anyone with non-public information materially related to a target security, obtained by virtue of a position within a given corporation, from dealing in that security.²⁴⁵ It is important to note that the Commission of the Stock Exchange, a group of experts composed of the leading financial institutions in Germany, drafted the traditional definition.²⁴⁶ While changing the legal system appears simple, changing the attitudes of the parties involved may prove more difficult. This paradox presents itself throughout consideration of the various German insider regulations.

While the German definition of insider is less inclusive than the British definition,²⁴⁷ several commentators debate its actual breadth.²⁴⁸ Essentially, the Insider Trading Guidelines apply only to employees, usually management, and stockholders who hold more than twenty-five percent of a company's shares.²⁴⁹ A few provisions apply to outside fi-

243. See Blum, *supra* note 223, at 519 (commenting on the importance of whether or not the exploited information is public); Rider, *supra* note 55, at 246 (stating that the definition of inside information hinges on whether or not the information was available to the public when used); see also Zahn, *supra* note 214, at 93 (noting that the Guidelines prohibit the use of inside information prior to publication).

244. See Hopt, *supra* note 212, at 384-86 (encouraging broadening the definition of insider trading in order to establish "certainty of law").

245. *Id.* at 385-86.

246. Comment, *New EEC Draft Directive*, *supra* note 38, at 128.

247. See *id.* (stating that the Guideline's definition of insider is less inclusive than the definition under the British Insider Act); Comment, *Harmonization of the Member States*, *supra* note 78, at 170-71 (noting that the German definition of insider is both less inclusive and more inflexible than either the British or French approaches).

248. See Rider, *supra* note 55, at 245 (noting that the Guidelines lack standards for determining which employees have insider status and that a company can unilaterally determine the insider status of its employees).

249. J. ROBINSON, *INTERNATIONAL SECURITIES LAW AND PRACTICE* 108 (1985) (citing *Insider Trading Directives as of 1976*, § 2(1)(a)-(d)). The Insider Trading Guidelines, provide in relevant part that insiders include:

- (a) legal representatives and members of the supervisory board of the company;
- (b) any such representatives of connected domestic companies;
- (c) domestic shareholders, including their legal representatives and supervisory board members, where they have more than a twenty-five percent interest in the company; and
- (d) employees of the company and of domestic companies connected with it and twenty-five percent shareholders in connected domestic companies.

Id.

duciaries such as banks or employees of a subsidiary.²⁵⁰

The German Guidelines do not cover secondary insiders, or tippees,²⁵¹ whom the EEC Directive addresses.²⁵² It is questionable whether the Guidelines permit all tippees to trade on privileged information.²⁵³ The grounds for this possible exception are found in the prohibition on insiders from trading "by virtue of their position."²⁵⁴

The Guidelines prohibit an insider from dealing in a stock if the stockbroker exploited insider information in making a trading decision.²⁵⁵ The Guidelines also prohibit an insider from dealing in order to benefit a third party.²⁵⁶ Moreover, while the Guidelines exclude tippees,²⁵⁷ they arguably prohibit tipping if the tipper deals through a third party.²⁵⁸

Finally, due to a perceived difficulty in international enforcement,²⁵⁹ basic prohibitions of the Insider Guidelines do not extend beyond Ger-

250. See *id.* at 109. These insiders include third parties "on equal footing" with the insider, such as banks, credit agencies, or other outside people whose positions allow them access to inside information. *Id.*

251. Council Directive, *supra* note 32, art. 4.

252. See *supra* note 181 and accompanying text (noting the importance that the EEC places on tippees); see Houle, *supra* note 150, at 219 (stating that if a person receives information in a way unrelated to her employment, then the Guidelines do not prohibit trading on that information); Hopt, *supra* note 212, at 384 (stating that the Guidelines exclude tippees).

253. See Hopt, *supra* note 212, at 396 n.27 (commenting that section 1 of the Guidelines, which prohibits insiders from trading by virtue of their position, may be given a narrow or broad interpretation).

254. *Id.* at 395 n.22 (citing *Insider Trading Guidelines*, § 1). The Insider Trading Guidelines provide that insiders may not trade using information obtained "by virtue of their position." *Id.*

255. *Id.* at 384; see Rider, *supra* note 55, at 245 (noting the prohibition that an insider may not use inside information to help him decide to deal for his own benefit).

The obligations imposed under the Guidelines, however, do not prohibit management personnel from owning or trading shares in their own company. Hopt, *supra* note 212, at 385. They simply cannot exploit inside information to their own benefit. *Id.*

256. See Hopt, *supra* note 212, at 384 (explaining *Insider Trading Guidelines* 1(1)); see also Houle, *supra* note 147, at 220 (stating that an insider may not trade for the benefit of a third-party); Rider, *supra* note 55, at 245 (stating that an insider may not deal with insider documents obtained by virtue of her position, in order to benefit a third party).

257. See *supra* notes 251-52 and accompanying text (noting that the Guidelines exclude tippees).

258. See Hopt, *supra* note 212, at 385 (noting that the extent to which the Guidelines prohibit an insider from tipping depends on whether that insider is tipping in order to make a deal through the tippee). Hopt also suggests that the tipper must "solicit" the third party's involvement in the deal. *Id.* If the third party acts independently, then the tipper does not violate the Guidelines. *Id.*

259. See *id.* (stating that international application would create enforcement problems).

man borders.²⁶⁰ The Guidelines also do not apply to a company's subsidiaries,²⁶¹ due to the inherent difficulty of forcing voluntary submission to rules.²⁶² This extraterritorial exception to a national prohibition on insider trading is consistent with the EEC Directive.²⁶³

D. ENFORCEMENT

Codifying national laws to prohibit insider trading is instrumental in providing a system of uniform regulation. Enforcement of prohibitions is paramount to determining a regulation's effectiveness. In the Federal Republic of Germany, review boards of the various stock exchanges enforce the Guidelines.²⁶⁴ These boards primarily ensure compliance with the Guidelines' rules²⁶⁵ by investigating the facts of a case.²⁶⁶ The review boards utilize several investigatory methods including inquiry, denunciation, and requests for documents from persons and institutions.²⁶⁷ The strength of the review board's suspicion determines the extent of the investigation.²⁶⁸ It is important to note, however, that sus-

260. See *id.* at 384 (stating that applying the voluntary Guidelines would hinder a parent company located overseas and other international business relationships).

261. See *id.* (speculating that the voluntary nature of the rules creates a significant problem with forcing a subsidiary to obey the prohibitions).

262. *Id.*

263. See *Council Directive, supra* note 32, art. 5, at 31 (providing for regulation insofar as a certain security is traded on a national exchange within a given country's border).

264. *Insider Trading Guidelines*, § 3 (as translated in Hopt, *supra* note 212, at 383). The review board consists of a president, four members and four deputies. Rider, *supra* note 55, at 246. The president of the Supreme Court nominates the president and his deputy and they are considered experienced in commercial matters. *Id.* The representatives then elect them from the various federations that participate in the regulatory scheme. *Id.* Finally, four other members and their deputies are elected from a pool of company representatives. *Id.* Two of the four members must have professional experience in the stock exchange. *Id.* A committee appointment lasts for three years. *Id.*; see also Hopt, *supra* note 212, at 390-91 (explaining the committee selection process).

265. Rider, *supra* note 55, at 246.

266. Hopt, *supra* note 212, at 383; see also Rider, *supra* note 55, at 246-47 (describing the Committee's investigatory function).

267. See Rider, *supra* note 55, at 246-47 (setting forth the various mechanisms through which the Committee can perform its duties).

268. See Hopt, *supra* note 212, at 391 (stating that if a strong suspicion exists that does not implicate any particular person or group, the Committee may obtain information from all relevant sources). This information might include where the party deposited the securities and which insider dealings the party may have performed with regard to the said securities. *Id.* An insider who the rules bind impliedly allows a bank to disclose relevant information concerning possible insider transactions. Houle, *supra* note 150, at 220. If the insider does not allow the bank to reveal the requested information, the Committee may take legal action against the insider to compel the disclosure. *Id.*

pected insiders and other persons with relevant information must willfully submit to the Guidelines in order to be subject to inquiry.²⁶⁹

If a violation has occurred, the accused must pay the costs incurred during the investigation.²⁷⁰ In the event of a violation, a report will be sent to the relevant parties involved, including the minister of the stock exchange.²⁷¹ Once the committee conducts the investigation, it sets forth final findings in writing.²⁷² As noted earlier, at this point the committee cannot make legal determinations or impose sanctions.²⁷³

The voluntary system in Germany may be less effective than a statutory scheme.²⁷⁴ The dearth of established insider abuse cases reported by review boards or in the financial press supports this contention.²⁷⁵ The desire for voluntary commitment, lower costs, and more flexibility, when compared to greater authority and equality obtained through access to the legal process, exemplify the underlying issues in the debate between voluntary and statutory insider trading regulatory schemes.²⁷⁶ Because the German system applies only to companies on the open market, it affects only one-fourth of all German stock corporations.²⁷⁷ It is, therefore, difficult to assert that the German system of enforcement is consistent with the principles set forth in the EEC Directive.

269. Hopt, *supra* note 212, at 391.

270. *See id.* at 391 (stating that the Committee decides to what extent it should assign costs); *see also* Rider, *supra* note 55, at 247 (stating that in the event of a breach, the accused must pay costs).

271. *See id.* at 390 (stating that these parties may include legal representatives of the company, members of the board of directors, presidents of relevant credit banks, as well as the minister of the affected stock exchange). Note that except in cases of gross abuse, communication to third parties requires consent from the insider. Rider, *supra* note 55, at 247. In cases of excessive abuse, however, the Committee may publish its findings without the accused's permission. Hopt, *supra* note 212, at 390.

272. *See* Rider, *supra* note 55, at 247 (stating that the Committee will give a formal written finding, prior to which the accused may defend himself or herself either in writing or by personal appearance).

273. *Supra* note 235 and accompanying text.

274. *See* Hopt, *supra* note 212, at 392 (favoring statutory regulation over self-regulation because both the hearings and the publication of the suspected offenses are public).

275. *See id.* at 391-92 (discussing cases involving several companies and hundreds of people in which the Committee suspected insider trading and rendered no finding of actual abuse, and also discussing the fact that the financial press has written on several insider cases, and reported no positive findings of abuse).

276. *See id.* at 392 (discussing the pros and cons of a voluntary versus a statutory system of securities regulation).

277. *Id.* at 392-93. As of 1985, only 450 German companies had shares trading on one of the national stock exchanges. *Id.* at 393. By the end of 1982, there were 2,140 stock companies and 350,000 companies with some liability. *Id.*

E. SANCTIONS AND PENALTIES

Criminal sanctions are not available under the German Insider Trading Guidelines.²⁷⁸ The legal nature of the insider provisions, however, does allow a company to pursue private action against an insider.²⁷⁹ In this regard, the most common sanction is disgorgement of all profits or transfer of assets acquired in avoiding a loss to the company with which the insider has established the requisite contractual relationship.²⁸⁰ The Guidelines do not consider civil remedies.²⁸¹

Unlike Great Britain, the Federal Republic of Germany needs to take significant steps to bring its insider trading regulations into accordance with the EEC Council Directive. The lack of German regulation of its securities industry creates the impression that it accepts the Guidelines as appropriate and effective. Additionally, Germany's small and less active markets may have an interest in not shaking investor confidence through strict and authoritative regulatory measures.²⁸² The cost of implementing regulatory devices also could easily outweigh benefits of uniform regulation in a relatively small market.²⁸³ As one prominent German commentator wrote in 1986, while the EEC Commission debated an insider trading directive, "[t]he attitude of the German professions is to reject the EEC's efforts; the German jurisprudence is still waiting."²⁸⁴

V. RECOMMENDATIONS

The European Community Council Directive is a substantial step toward the creation of uniform regulation of insider trading. Its success or failure depends on two key elements. First, the individual Member

278. Houle, *supra* note 150, at 221; *see also* Hopt, *supra* note 212, at 388 (positing that criminal law cannot enforce the Guidelines because the provisions are non-statutory, unofficial, and unsanctioned in nature).

279. *See supra* notes 235, 238 and accompanying text (discussing a company's private right of action).

280. *See* Hopt, *supra* note 212, at 388 (stating that a transfer of all assets made during the illegal dealings to the company for whom the insider worked is the usual form of sanction).

281. *See id.* at 389 (stating that the Guidelines neither include nor exclude civil actions). In stock market deals, the trader benefits, while the company being traded suffers no material harm. *Id.* Moreover, everyone else who traded at the skewed market rate has no identifiable recourse. *Id.* Thus, the company being traded on insider information for "transfer of profits" would be most likely to bring a civil suit. *Id.*

282. Kubler, *supra* note 5, at 114.

283. *Id.*

284. Hopt, *supra* note 212, at 393. Hopt also noted that Germany has harmonized some laws with other securities directives and that a proposed insider directive would likely leave the choice of sanctions to the Member States. *Id.* at 393-94.

States must realize the benefits of the exchange of information and the potential for broad-based cooperation. Additionally, Member States, especially those which have not yet codified insider trading prohibitions, must implement comprehensive enforcement provisions and severe sanctions to deter illegal dealing.

As the EEC—a free-trade zone consisting of twelve independent nations—is particularly susceptible to transnational insider trading, the exchange of information required by Article 8 and 10 of the Council Directive is crucial.²⁸⁵ While the Directive does mention international cooperation in the Preamble and in three separate Articles, words alone will not solve the mutual exchange problems between twelve independent states. The establishment of a regulatory body, the “contact committee,” will therefore greatly enhance the prospect for free exchange of information. To be effective, however, this body must have the authority to determine when information might compromise the sovereignty, security, or public policy of a particular Member State. To allow the Member States to avoid cooperation based on a pretext of sovereignty, security, or public policy would frustrate the clear intent of the Council Directive.

Provision of some degree of central authority and guidance can address the second major consideration, comprehensive enforcement and adequate sanctions. While this may compromise the Directive's principles of self-implementation and enforcement, Member States should seek to have a central information center for gathering and analyzing relevant market information from all twelve markets. This central authority also should possess the power to conduct full-scale investigations.²⁸⁶ In order to preserve sovereign integrity, each Member State would carry out any criminal or civil proceeding under its own insider laws.

Finally, a strict and widely recognized set of criminal and civil sanctions is necessary in order to realize the Directive's goals of uniform investor protection.²⁸⁷ An insider must not feel “safer” in some Member States than in others. If this were the case, then the overall situation would remain substantially unchanged. The most direct and effec-

285. *Supra* note 105 and accompanying text.

286. *See supra* notes 38-47 and accompanying text (stressing the importance of uniform law and investor protection in meeting the EEC's economic goals). A common investigatory scheme would prevent an insider in one country from being under less scrutiny than an insider in another Member State, thus furthering the goals of EEC market interpretation.

287. *See supra* notes 118-19, 121-22 and accompanying text (discussing sanctions under the Directive).

tive means of accomplishing uniform provisions would be to amend the Council Directive.²⁸⁸

CONCLUSION

An analysis of the insider trading provisions in the United Kingdom and The Federal Republic of Germany has significant implications for determining the future success of the EEC Directive. As the United Kingdom regulations are highly codified and served as a model for the Directive,²⁸⁹ British success or failure in dealing with insider trading is indicative of expectations for the EEC.²⁹⁰ The "scienter" requirement employed in British insider regulations,²⁹¹ as well as its statutory defenses²⁹² and lackluster enforcement record,²⁹³ indicate that treatment of insider trading in the United Kingdom is not only different from the EEC's provisions, but also has not been completely successful. Those Member States that implement provisions similar to the British statutes in response to the Directive's requirements may find similar difficulties in realizing their intended goals.

As for the treatment of insider trading in Germany, an analysis must consider several factors in determining the prospects for success of the EEC Directive. While there is some room for interpretation of the Guidelines, the basic prohibition of dealing on inside information set forth in the EEC Directive appears to exist. The Germans will have to re-work their prohibitions on tipping, however, in order to meet the criteria set forth in the Council Directive. This may be an arduous task,

288. Amending the Directive to provide for an express private right of action would greatly enhance its effectiveness. In the United States, for example, the courts have developed a private cause of action under section 10(b) of the Securities Act of 1934, and Rule 10b-5 promulgated thereunder. *Herman & MacLean v. Huddleston*, 459 U.S. 375, 380 (1983). Many widely recognize this private cause of action as a necessary and valuable compliment to the regulatory scheme that the SEC administers. See Note, *In Pari Delicto and Insider Trading: Dead or Alive?*, 52 BROOKLYN L. REV. 1169, 1175, 1198 (1987) (noting that both the Supreme Court and the SEC have reasoned that the private right of action is a necessary supplement to the Commission's enforcement operation); see also, Note, *Private Causes of Action for Option Investors Under SEC Rule 10b-5: A Policy Doctrinal, and Economic Analysis*, 100 HARV. L. REV. 1959, 1963 (1987) (stating that the private cause of action under Rule 10b-5 buttresses SEC enforcement and provides a crucial deterrence mechanism necessary in securities transactions). As the private cause of action has been effective in United States regulatory efforts, utilizing this method of investor protection should compliment the Directive's statutory provisions as well.

289. *Supra* note 78 and accompanying text.

290. See Rider, *supra* note 55, at 243 (asserting that British regulation has significant impact on the prospects for Community-wide success).

291. See *supra* note 167 and accompanying text (discussing British insider laws).

292. *Supra* notes 182-83 and accompanying text.

293. *Supra* notes 205-07, 210-11 and accompanying text.

as most major German financial institutions participated in the creation of the original guidelines and have maintained their support for the initial provisions.²⁹⁴

A further consideration in determining the prospects for future regulatory success is that the voluntary Guidelines may reflect German attitudes toward insider regulations in general. If this is the case, significant philosophical and legal changes will have to occur. The EEC Directive requires the Member States to establish competent administrative authorities to regulate insider trading,²⁹⁵ and at this point the German scheme is neither nationally enforced nor administrative in nature.

Germany is not unique. Seven other Member States do not have statutory regulations prohibiting insider trading.²⁹⁶ The same factors that have affected the German attitude towards insider regulations, relatively small markets and the expense of implementing advanced regulatory mechanisms,²⁹⁷ may indeed affect other countries of the EEC as well, and hinder the ultimate goal of an advanced, integrated system of regulations, replete with mutual cooperation and a uniform level of investor protection.

294. *Supra* notes 231-34 and accompanying text.

295. *Council Directive*, *supra* note 32, art. 8.

296. *Supra* notes 21-22 and accompanying text.

297. *Supra* notes 282-83 and accompanying text.