Florida Journal of International Law

Volume 11 | Issue 1 Article 7

September 1996

The New German Insider Law: Introduction and Discussion in Relation to United States Securities Law

Peter M. Memminger

THE NEW GERMAN INSIDER LAW: INTRODUCTION AND DISCUSSION IN RELATION TO UNITED STATES SECURITIES LAW

*Peter M. Memminger**

* J.D. Candidate, Oct. 1998, University of Freiburg School of Law (Germany); LL.M., Dec. 1998, University of Miami School of Law. Some editing assistance was provided by Mark L. Pateman, J.D., University of Miami School of Law; B.A., Skidmore College. Mr. Pateman was the Executive Editor for the University of Miami Yearbook of International Law, 1996-1997. He now is an attorney with the New York law firm of Cadwalader, Wickersham & Taft. I would like to thank Professor Samuel C. Thompson, Dean of the University of Miami School of Law for his assistance and guidance.

I. INTRODUCTION

On July 26, 1994, the German parliament adopted the Second Financial Market Promotion Law (*Zweites Finanzmarktförderungsgesetz*[1]), which is described as the most important reform of the German financial market in the last one hundred years because of its severe impact on various stock exchange and capital market related acts.[2] With its enactment, the German legislature began to regulate insider trading for the first time in German history. The insider trading provisions are thereby included in the German Securities Trading Act (Wertpapierhandelsgesetz) (WpHG),[3] which is contained in article one of the Second Financial Markets Promotion Law.

With respect to the German Securities Trading Act's decisive influence on both the trading activities and investment counseling practices of brokers and banks, combined with the Act's implications on the standard of conduct of listed corporations, few articles written in English[4] have discussed the

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1. The full title is: Gesetz über den Wertpapierhandel und zur Änderung börsenrechtlicher und wertpapierrechtlicher Vorschriften (Act on Securities Trading and for the Modification of Regulations Governing the Stock Exchanges and Securities) (Zweites Finanzmarktförderungsgesetz) (Second Financial Market Promotion Law), v.26.7.1994 (BGBl. I S.1749).

2. It affected, for example, the Stock Exchange Act, the Securities Sales Prospectus Act, the Stock Corporation Act, the Commercial Code, and the Insider Guidelines.

3. Zweites Finanzmarktförderungsgesetz, art. 1, Gesetz über den Wertpapierhandel Art. (Wertpapierhandelsgesetz) (Securities Trading Act), v.26.7.1994 (BGBl. I S.1750-60) [hereinafter WpHG]. An English translation of the Act can be ordered from the Bundesaufsichtsamt für den Wertpapierhandel (Federal Supervisory Authority) in Frankfurt/Main, Germany.

4. The following articles have at least partially addressed the German Securities Trading Act. TONY HICKINBOTHAM & CHRISTOPH VAUPEL, INTERNATIONAL INSIDER DEALING, GERMANY PART 129 (Stamp Welsh ed. 1996); KONRAD MOHR, GERMAN INSIDER AND STOCK EXCHANGE LAW (1995); Eberhard H. Röhm, *Germany, in* 10A INTERNATIONAL CAPITAL MARKETS AND SECURITIES REGULATION § 8C.11 (Harold S. Bloomenthal ed., Clark Boardman Callaghan Series 1991); Joseph Blum, *The Regulation of Insider Trading in Germany: Who's Afraid of Self-Restraint?*, 7 NW. J. INT'L L. & BUS. 507 (1986); Christof von Dryander, *The German Securities Trading Act: Insider Trading and Other Secondary Market Regulation*, 9(1) INSIGHTS 26 (1995); James H. Freis, Jr., *An Outsider's Look into the Regulation of Insider Trading in Germany: A Guide to Securities, Banking, and Market Reform in Finanzplatz Deutschland*, 19 B.C. INT'L & COMP. L. REV. 1 (1996) (also providing a general overview of the regulatory scheme of the German financial markets); Ursula C. Pfeil, *Finanzplatz Deutschland: Germany Enacts Insider Trading Legislation*, 11 AM. U. J. INT'L L. & POL'Y 137 (1996); Harvey L. Pitt & David B. Hardison, *Games Without Frontiers: Trends in the International Response to Insider Trading*, 55 LAW & CONTEM. PROBS. 199 (1992); Hans-Bernd Schäfer & Claus Ott, *Economic Effects of EEC Insider Trading Regulation Applied to Germany*, 12 INT'L REV. L. & ECON. 357 (1992) (for data materials regarding detected insider violations in Germany prior to the Securities Trading Act's enactment); Daniel James Standen, *Insider Trading Reforms Sweep Across Germany: Bracing for the Cold Winds of Change*, 36 HARV. INT'L L.J. 177 (1995); Symposium, *New Approaches to Securities Regulation*, 29 INT'L LAW. 839 (1995). All of the articles above have covered the Securities Trading Act, without,

importance of this Act. Most cover a wide range of provisions of the German Securities Trading Act without focusing in detail on the insider dealing sections. In contrast, scholarly work on this subject written in German is quite extensive.[5]

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however, providing guidance in detail questions.

5. *See* ARBEITSKREIS GESELLSCHAFTSRECHT, VERBOT DES INSIDERHANDELS [PROHIBITION OF INSIDER TRADING] (1976); KLAUS DIETER ASSMANN & UWE H. SCHNEIDER, WERTPAPIERHANDELSGESETZ [COMMENTARY TO THE SECURITIES TRADING ACT] (1995); JOACHIM BECKER, DAS NEUE WERTPAPIERHANDELSGESTZ [THE NEW SECURITIES TRADING ACT] (1995); CARSTEN PETER CLAUSSEN, BANK- UND BÖRSENRECHT [BANK AND SECURITY EXCHANGE LAW] (1996); DEUTSCHE BÖRSE AG, INSIDERHANDELSVERBOTE UND AD-HOC PUBLIZITÄT NACH DEM WERTPAPIERHANDELSGESETZ [INSIDER TRADING PROHIBITION AND AD-HOC PUBLICITY ACCORDING TO THE SECURITIES TRADING ACT] (1994); SIEGFRIED KÜMPEL, BANK- UND KAPITALMARKTRECHT [BANKING AND FINANCIAL MARKET LAWS] (1995); HANNS CHRISTOPH SIEBOLD, DAS NEUE INSIDERRECHT: VON DER FREIWILLIGEN SELBSTKONTROLLE ZUM INTERNATIONALEN STANDARD [THE NEW INSIDER LAW: FROM FREE-WILLED SELF-CONTROL TO THE INTERNATIONAL STANDARD] (1994); Heinz-Dieter Assmann, *Das künftige deutsche Insiderrecht (I)* [*The Forthcoming German Insider Law (I)*], DIE AKTIENGESELLSCHAFT [AG], June 1994, at 196 [hereinafter Assman, *Part I*]; Heinz-Dieter Assmann, *Das künftige deutsche Insiderrecht (II)* [*The Future German Insider Law, (II)*], AG, June 1994, at 237 [hereinafter Assman, *Part II*]; Heinz-Dieter Assmann, *Das neue deutsche Insiderrecht* [*The New German Insider Law*], ZEITSCHRIFT FÜR UNTERNEHMENS- UND GESELLSCHAFTSRECHT [ZGR], 1994, at 494 [hereinafter Assmann, *The New German Insider Law*]; Jella Benner-Heinacher, *Kollidiert die Auskunftspflicht des Vorstands mit dem Insidergesetz?* [*Is the Reporting Duty of the Management Board in Collision with the Insider Law?*], DER BETRIEB [DB], 1995, at 765; Karl-Burkhard Caspari, *Die geplante Insiderregelung in der Praxis* [*Practical Aspect of the Planned Insider Law*], ZGR, 1994, at 530; Carsten P. Claussen, *Das neue Insiderrecht* [*The New Insider Law*], DB, 1994, at 27; Markus Gehrlein, *Die geltende deutsche Insiderregelung* [*The Actually Effective German Insider Regulation*], DIE WIRTSCHAFTLICHE BERATUNG [WiB], 1994, at 344; Klaus J. Hopt, *Europäisches und deutsches Insiderrecht* [*European and German Insider Law*], ZGR, 1991, at 17 [hereinafter Hopt, *European & German Insider Law*]; Klaus J. Hopt, *Rechtsprobleme des europäischen und deutschen Insiderrechts* [*Legal Problems Under the European and German Insider Law*], BETRIEBSWIRTSCHAFTLICHE FORSCHUNG UND PRAXIS [BFuP], 1994, at 85 [hereinafter Hopt, *Legal Problems*]; Klaus J. Hopt, *Grundsatz- und Praxisprobleme nach dem Wertpapierhandelsgesetz* [*Basic and Practice Problems Under the Securities Trading Act*], ZEITSCHRIFT FÜR DAS GESAMTE HANDEL- UND GESELLSCHAFTSRECHT [ZHR], 159 (1995), at 135 [hereinafter Hopt, *Basic Problems*]; Frank A. Immenga, *Das neue Insiderrecht im Wertpapierhandelsgesetz* [*The New Insider Law of the Securities Trading Act*], ZEITSCHRIFT FÜR BANKRECHT UND BANKWIRTSCHAFT [ZBB], 1995, at 197; Klaus H. Jander & Manuela Zoberbier, *Das Zweite Finanzmarktförderungsgesetz mit der Neuregelung des Insiderrechts* [*The Second Financial Markets Promotion Act with the New Regulation of the Insider Law*], WIB, 1994, at 806; Peter Joussen, *Auskunftspflicht des Vorstandes nach § 131 AktG und Insiderrecht* [*The Reporting Duty of the Management Board Under AktG, Section 131, and Insider Law*], DB, 1994, at 2485; Siegfried Kümpel, *Die künftige Kapitalmarktaufsicht und die europäische Rechtsangleichung* [*The Future Financial Markets Supervision and the European Harmonization of Law Process*], DIE WERTPAPIERMITTEILUNGEN [WM], 1994, at 229 [hereinafter Kümpel, *Financial Markets Supervision*]; Siegfried Kümpel, *Zum Begriff der Insidertatsache* [*The Term Inside Information*], WM, 1994, at 2137 [hereinafter Kümpel, *Inside Information*]; Andreas Möller, *Das neue Insiderrecht — Eckpfeiler funktionsfähiger Wertpapiermärkte* [*The New Insider Law — Essential Supporting Beam for Functional Securities Markets*], BFuP, 1994, at 99; Martin Peltzer, *Die neue Insiderregelung im Entwurf des Zweiten Finanzmarktför-*

The purpose of this article is to provide an in-depth analysis of the suppressive provisions of the Act, as well as to illustrate its notification provisions through which the danger of criminal prosecution can be diminished. Moreover, where it seems appropriate for clarity and contrast, this article will refer to the U.S. counterparts of the Act's fundamental regulations. Consequently, part II briefly focuses on the developments leading to the enactment of the Act, and part III provides a concentrated illustration of the Act's major provisions such as suppressive[6] and preventive[7] measures, and the establishment of a continuous supervision system.[8] It also contains a comprehensive discussion and analysis of the Act's central definitions and concepts such as "inside information,"[9] "insider,"[10] "insider securities,"[11] and "prohibition of insider dealing."[12] This part discusses the application of the relevant provisions to professional groups, such as stockbrokers, security analysts, and employees of issuers, with regard to their respective obligations. The reporting and disclosure duties of the Act are discussed in part IV. Finally, the article concludes with an evaluation of insider regulation under the Act.

II. BACKGROUND/DEVELOPMENTS PRIOR TO ENACTMENT

Before the Securities Trading Act became effective, in 1970, the German legislature had attempted to prevent insider trading with the promulgation of the Insider Trading Guidelines[13] last revised in 1988. The Guidelines were

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derungsgesetzes [*The New Insider Regulation in the Draft Bill of the Second Financial Markets Promotion Act*], ZIP, 1994, at 746; Klaus Rellermeyer, *Das Zweite Finanzmarktförderungsgesetz in der praktischen Umsetzung* [*The Second Financial Markets Promotion Act and Its Adoption in the Practice*], WM, 1995, at 1981; Hans-Joachim Schwarze, *Insideregelung im Spannungsfeld der Praktikabilität* [*Insider Regulation and the Conflict with Their Practicability*], BFuP, 1994, at 124; Martin Weber, *Deutsches Kapitalmarktrecht im Umbruch* [*German Capital Market Law in a Changing Situation*], NEUE JURISTISCHE WOCHENZEITSCHRIFT [NJW], 1994, at 2849 [hereinafter Weber, *Changing Situation*]; Ulf Andreas Weber, *Das neue deutsche Insiderrecht* [*The New German Insider Law*], BB, Jan. 1995, at 157 [hereinafter Weber, *The New German Insider Law*].

6. Suppressive measures are contained in § 14 (Prohibition of Insider Dealing), § 18 (Criminal Proceedings in Cases of Insider Violations), and §§ 38-40 (Criminal Offense and Misdemeanor Provisions) of the WpHG. WpHG §§ 38-40, v.26.7.1994 (BGBl. I S.1753, 1754, & 1759-60, respectively).

7. Preventive regulations are especially the public disclosure and reporting duties under WpHG. *Id.* § 15, at S.1753-54.

8. *Id.* § 16, at S.1754 (Continuous Supervision).

9. *Id.* § 13, at S.1753.

10. *Id.*

11. *Id.* § 12, at S.1753.

12. *Id.* § 14, at S.1753.

13. *Insiderhandelsrichtlinien* (Insider Trading Guidelines), WM, 1988, at 1066ff. *See* SIEBOLD, *supra* note 5, at 57, and Blum, *supra* note 4, at 507 for more information with regard to these Guidelines.

generally regarded as quite ineffective, since they neither had the legal authority of an enacted law, nor were they accepted by courts as trade practice.[14] Rather, the Insider Trading Guidelines presented a set of voluntary rules of conduct that could only become legally binding through their inclusion in private contracts.[15] Theoretically, a violation of such a contractual arrangement could be pursued under certain laws relating to economic offenses.[16] In practice, however, violations of the Guidelines were very rarely detected and only resulted in damages for breach of a contractual obligation.[17]

Moreover, the board of inquiry that supervises conformity with the Insider Trading Guidelines had limited investigative authority. For instance, it was not allowed to seize evidence, and inquiries about suspicious trading activities had to be approved by the involved parties.[18] As a consequence, this voluntary system of self-control was widely criticized for its inefficiency. Scholarly publications[19] called for statutory regulations prohibiting insider transactions, referring to the insider laws of many other countries with major capital markets like the United States and Great Britain. However, the critics of the self-regulating system could not prevail over the system's proponents because until the end of the 1980s, Germany lacked the scandalous and big insider cases that would have attracted the attention of a wider spectrum of investors.[20]

This situation changed with the enactment of a European Union (EU) Council Directive[21] in November 1989, which did not directly prohibit insider trading, but rather contained specific regulations that had to be implemented by the EU member states, with the intention of eroding insider activities. Faced with this directive and the perception that the German financial market was less attractive to international investors due to, among other reasons, the lack of insider dealing regulation, the German legislature

14. *See* Pitt & Hardison, *supra* note 4, at 199.

15. Gehrlein, *supra* note 5, at 344; Pfeil, *supra* note 4, at 141.

16. For example, § 404(2) of the Aktiengesetz (Corporation Act). Aktiengesetz (Corporation Act) § 404(2), v.6.9.1965 (BGBl. I S.1089-1185) [hereinafter AktG].

17. Gehrlein, *supra* note 5, at 345; Standen, *supra* note 4, at 197.

18. Jander & Zoberbier, *supra* note 5, at 806; Pfeil, *supra* note 4, at 142.

19. As an example, *see Gesetzesentwurf zum Insiderhandel des Arbeitskreis Gesellschaftsrecht [Proposal of an Insider Trading Act from the Arbeitskreis Gesellschaftsrecht], in* ARBEITSKREIS GESELLSCHAFTSRECHT, *supra* note 5, at 55.

20. Assmann, *Part I*, *supra* note 5, at 198. For data on detected insider trades under the Insider Trading Guidelines, *see* Schäfer & Ott, *supra* note 4.

21. EU, Council Directive 89/592, Coordinating Regulations on Insider Dealing, 1989, O.J. (L334) 30; *see* Lynda M. Ruiz, *European Community Directive on Insider Dealing: A Model for Effective Enforcement of Prohibitions on Insider Trading in International Securities Markets*, 33 COLUM. J. TRANSNAT'L L. 217, 235-39 (1995).

ultimately took action and adopted the Securities Trading Act.[22] The German parliament describes the purpose of the Act as the improvement of the attractiveness and international competitiveness of the German financial markets by increasing investor protection and broadening the availability of material corporate information.[23] This goal was crucial to the strength of the German capital markets since the international financial markets had become more and more competitive. Consequently, governmental regulations play an increasingly decisive role in investment decisions.[24] Since investors look carefully at the equal availability of corporate information as a basic component of fair investment chances, insider trading prohibitions were essential for fulfilling the demands of these groups and thereby providing German corporations with needed capital.[25]

III. ANALYSIS

A. *Structure*

The structure of the Securities Trading Act can be divided into provisions designed to avoid insider trading through the prohibition and criminal prosecution of insider dealing (suppressive measures), those that establish public disclosure and reporting duties (preventive measures), and those that establish a system of continuous market supervision.

1. Suppressive Provisions and Preventive Measures

The essential suppressive measure of the Securities Trading Act is undoubtedly the insider trading prohibition.[26] The scope of this provision is determined by the term "insiders," which is defined as persons who (1) as members of the supervisory[27] or management[28] body, (2) as shareholders or partners of the issuer,[29] or (3) by reason of their profession or employment relationship, have, in due course, obtained knowledge of inside

22. CLAUSSEN, *supra* note 5, § 9 n.9; Dryander, *supra* note 4, at 26; Immenga, *supra* note 5, at 199.

23. This is a nonexclusive enumeration. Other measures for improving the quality of the German financial markets include the removal of certain limitations in the Corporation Act, as well as in the Securities Deposit Act. *See* Freis, *supra* note 4, at 37.

24. Gesetzesentwurf (draft bill) Zweites Finanzmarktförderungsgesetz, BUNDESTAG-DRUCKSACHE 12/6679, at 33 [hereinafter BT-DRUCKS] (explanation of the Federal government).

25. *Id.*

26. WpHG § 14, v.26.7.1994 (BGBl. I S.1753).

27. *Id.* § 13(1)1., at S.1753 (*Aufsichtsorgan* translates as supervisory body).

28. *Id.* (*Geschäftsführungsorgan* translates as management body).

29. *Id.* § 13(1)2., at S.1753.

information[30] (the primary insiders).[31] In addition to these specific groups, anyone else who has knowledge of inside information and cannot be assigned to one of the above presented groups also qualifies as an insider[32] (the secondary insider).[33]

The distinction between primary and secondary insiders is especially important with regard to their respective obligations under the insider trading prohibition. Primary insiders are subject to a threefold exploitation restriction of their inside knowledge. First, trading in inside securities,[34] whether for their own account or that of a third party, is prohibited.[35] Second, a primary insider shall not convey his inside information to another person.[36] Finally, a primary insider is precluded from recommending the purchase or sale insider securities to another person[37] In U.S. law this is known as tipper/tippee liability. In contrast, secondary insiders merely are subject to a utilization prohibition of their knowledge, which includes the restriction on the sale or purchase of insider securities for their account or the account of a third party.[38]

A primary or secondary insider is someone who is in the possession of inside information.[39] "Inside information" is defined as "information which has not been made public relating to one or more issuers of insider securities, or to inside securities, which if it were made public, would be likely to have a significant effect on the price of the insider security."[40] Violations of the insider trading prohibition are prosecuted under the sections of the Act that

30. *Id.* § 13(1)3., at S.1753.

31. The term "primary insider" is not used in the text of the Act itself, but it can be concluded from the structure of the Act (the distinction between insiders and third persons who have knowledge of inside information) that "primary insiders" are the group of people who are the insiders in the Act. Consequently, "secondary insiders" are the "third persons with knowledge of inside information." Indeed, the federal government used the terms primary and secondary insider in its explanation to the proposed bill, BT-DRUCKS, *supra* note 24, at 46, in the same context as defined here. Since most of the scholarly publications also are based on this terminology, this article will follow their usage.

32. WpHG § 14(1)2., v.26.7.1994 (BGBl. I S.1753).

33. "Secondary insiders" is equivalent to "third persons with knowledge of inside information" named in the Act. *Id.; see supra* text accompanying note 31.

34. WpHG § 12, v.26.7.1994 (BGBl. I S.1753) (defining insider securities). For further discussion, *see infra* part III.B.3.

35. WpHG § 14(1)1, v.26.7.1994 (BGBl. I S.1753).

36. *Id.* § 14(1)2., at S.1753.

37. *Id.* § 14(1)3., at S.1753.

38. *Id.* § 14(2), at S.1753.

39. *Id.* § 13(1), at S.1753.

40. *Id.* The original German formulation is "*Kenntnis von einer nicht öffentlich bekannten Tatsache hat, die sich auf einen oder mehrere Emittenten von Insiderpapieren oder auf Insiderpapiere bezieht und die geeignet ist, im Falle ihres öffentlichen Bekanntwerdens den Kurs der Insiderpapiere erheblich zu beeinflußen (Insidertatsache).*" *Id.*

deal with criminal proceedings.[41] These regulations are discussed later in this article.[42]

In addition to the above mentioned provisions that are designed to deter potential insiders, the Securities Trading Act has instituted a duty for issuers of securities to publish and report information,[43] which could affect the price of those securities in realization that the basic precondition for profitable insider trade is the imbalance of knowledge among market participants.[44] The Act intends to create equal access to market knowledge through an early publication of inside information. The central point thereof is the publication and reporting duty of price-sensitive information first to a Federal Supervisory Authority[45] and then to the public[46] (ad-hoc publicity).[47]

2. Market Supervision

The German Securities Trading Act establishes a new system of market supervision with broad investigative powers for the federal authorities. It thereby intends to supervise not only the enforcement of the insider trading law, but also the reporting and disclosure duties. Supervision of the insider trading prohibition is the duty of the newly created Federal Supervisory Authority.[48] This agency is directly subordinate to the Federal Ministry of Finance.[49] Organizational matters and obligations of the Federal Supervisory Authority, such as cooperation with comparable foreign agencies, are regulated in WpHG, Sections 3 through 11. Accordingly, in addition to revealing insider violations, the Federal Supervisory Authority supervises

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41. *Id.* §§ 38-40, at S.1759-60 (Criminal Offense and Misdemeanor Provisions).

42. *See infra* part IV.C.

43. WpHG § 15, v.26.7.1994 (BGBl. I S.1753-54) (*Veröffentlichung und Mitteilung kursbeeinflußender Tatsachen*) (Publication and Reporting of Price-Sensitive Information) [hereinafter Ad-Hoc Publicity].

44. Assmann, *The New German Insider Law*, *supra* note 5, at 527-28; Immenga, *supra* note 5, at 205.

45. The German *Bundesaufsichtsamt für den Wertpapierhandel* translates as Federal Securities Trading Supervisory Authority [hereinafter Federal Supervisory Authority]. *See* WpHG § 3, v.26.7.1994 (BGBl. I S.1750). More details about this agency are provided *infra* part III.B.3.

46. *See* BECKER, *supra* note 5, at 78; DEUTSCHE BÖRSE AG, *supra* note 5, at 13.

47. WpHG § 15, v.26.7.1994 (BGBl. I S.1753-54). This article mostly focuses on the suppressive measures of the Securities Trading Act. A brief introduction to the reporting and disclosure duties arising from § 15 (Ad-Hoc Publicity) and § 21 (*Mitteilungspflichten des Meldepflichtigen*) (Notification Requirements Applicable to the Notifying Party) is provided *infra* part IV.A & B.

48. WpHG § 16, v.26.7.1994 (BGBl. I S.1754) (*Laufende Überwachung*) (Continuous Supervision).

49. *Id.* § 3, at S.1750.

compliance with the ad-hoc publicity requirement[50] and the reporting and publication obligation in case of changes in the holdings of voting rights in exchange-listed companies.[51] Regarding certain requirements, the Federal Supervisory Authority may consult with the domestic supervisory authorities of regional exchanges.[52]

The presuppositions for the detection of insider violations are established by reporting obligations of banks[53] with regard to each securities transaction and by the insider violation information rights[54] of the Federal Supervisory Authority. In order to supervise security issuers, the Federal Supervisory Authority also has information rights against them.[55] Security issuers must comply with other reporting obligations, as well.[56]

German credit institutions, foreign credit institutions having a German registered office or branch, and all foreign enterprises admitted to participate in a German security exchange are required to report to the Federal Supervisory Authority each transaction in securities or derivatives that is admitted to over-the-counter trading[57] or to a security exchange in Germany, in the European Union, or in the European Economic Area.[58] Furthermore, this obligation also applies to transactions for which an application for admission to trading on these markets of the involved shares or warrants has been made or publicly announced.[59] Inasmuch as the Federal Supervisory Authority has reason to believe that a violation of the insider trading prohibition has occurred, it may require the involved banks and corporations[60] to provide information regarding the suspicious transaction and the parties involved.[61] Based on this information right, the Authority is permitted to enter the business office and premises of involved credit

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50. *Id.* § 15, at S.1753-54.

51. *Id.* § 21, at S.1755; *see* CLAUSSEN, *supra* note 5, § 9; SIEBOLD, *supra* note 5, at 255; Kümpel, *Financial Markets Supervision*, *supra* note 5, at 230; Weber, *Changing Situation*, *supra* note 5, at 2850.

52. The supervisory authorities include, for example, the exchange supervisory authorities of the regional securities exchanges and the *Bundesaufsichtsamt für das Kreditwesen* (Federal Banking Supervisory Authority). WpHG § 6, v.26.7.1994 (BGBl. I S.1751-52). For more details with regard to the organization of the German financial markets, *see* Freis, *supra* note 4, at 6-7.

53. WpHG § 9, v.26.7.1994 (BGBl. I S.1751-52).

54. *Id.* § 16(2) at S.1754.

55. *Id.* § 15(5), at S.1754.

56. This refers to the reporting obligations under § 15(2) & (4). *Id.* § 15(2) & (4), at S.1753-54.

57. *Freiverkehrsmarkt* includes over-the-counter trading or unlisted trading.

58. *Europäischer Wirtschaftsraum* (European Economic Area).

59. *Id.* § 9(1) sentence 2, at S.1752; *see also* Assmann, *The New German Insider Law*, *supra* note 5, at 526; Peltzer, *supra* note 5, at 752.

60. The credit institutions and enterprises within the meaning of § 2(4)1. WpHG § 2(4)1., v.26.7.1994 (BGBl. I S.1750).

61. *Id.* § 16(2)-(3), at S.1754.

institutions and enterprises.[62] Moreover, persons with actual knowledge of inside information and issuers of insider securities (and their associated enterprises) are required upon request to furnish the Authority with data about this information and about persons who might have knowledge of this information.[63] All persons, so identified, must then deliver the information to the Authority.[64] It is important to note, however, that the Act provides the right to withhold facts whose release would harm the above mentioned persons or their relatives.[65]

The penalties for violations of the Securities Trading Act vary according to whether a violation qualifies as a misdemeanor or a criminal offense. According to Section 39, violations of the ad-hoc publicity requirements, as well as the refusal to provide information or to permit entry into business offices,[66] constitute a misdemeanor.[67] As such, they are punishable with an administrative fine[68] of up to DM3,000,000.[69] The Federal Supervisory Authority is the competent administrative authority obligated with the detection and prosecution of misdemeanors.[70]

Contraventions of the insider trading prohibition qualify as a criminal offense.[71] Accordingly, they are punishable with a fine or with imprisonment for up to five years. The Act does not distinguish between violations committed by a primary insider and those committed by a secondary insider. This equal treatment, in addition to the strict sanctions, are evidence of a change of position by the German legislature: insider trading can no longer be regarded as a gentleman's offense, but rather must be viewed as harmful as fraud or similar dishonest dealings.[72] When compared with other European countries, Germany has enacted one of the most stringent punishment regulations.[73] If any circumstance gives rise to suspicion of a violation of the insider trading prohibition, the Federal Supervisory Authority is required to notify the competent public prosecutor's office,[74] which then

62. *Id.* § 16(3), at S.1754.
63. *Id.* § 16(4), at S.1754.
64. *Id.* § 16(5), at S.1754.
65. *Id.* § 16(6), at S.1754. For the conditions under which the right to withhold information exists, *see* Siebold, *supra* note 5, at 263.
66. Both of them are required under § 16. WpHG § 16, v.26.7.1994 (BGBl. I S.1754).
67. *Id.* § 39, at S.1759.
68. *Geldbuße* (administrative fine).
69. *Id.* § 39(3), at S.1760; ASSMANN & SCHNEIDER, *supra* note 5, § 39 para. 1.
70. WpHG § 40, v.26.7.1994 (BGBl. I S.1760); Assmann, *The New German Insider Law*, *supra* note 5, at 527; Jander & Zoberbier, *supra* note 5, at 810.
71. WpHG § 38, v.26.7.1994 (BGBl. I S.1759).
72. *Betrug* (fraud); *Untreue* (dishonest dealing). *See* BECKER, *supra* note 5, at 75.
73. For more information, *see* SIEBOLD, *supra* note 5, at 271.
74. *Staatsanwaltschaft* (public prosecutor's office).

is in charge of further proceedings and investigations.[75] An important factor is the possibility under the Act of punishing violations by German citizens in foreign countries of insider trading prohibitions under the same German standard as domestic contraventions.[76]

B. *Definitions and Concepts*

1. Inside Information

An essential term of the Securities Trading Act is "inside information." According to Section 13(1), "inside information" is defined as "information which has not been made public relating to, or to one or more issuers of, insider securities which, if it were made known to the public, would be likely to have a significant effect on the price of the insider security."[77] Without the ability to qualify data as inside information, all of the Act's other provisions relating to the insider trading prohibition cannot come into play. Therefore, a detailed discussion is necessary to clarify, with relative certainty, the legal meaning of this term.

"Information," as defined by the Act, is information about events or circumstances that can be objectively scrutinized and verified. As such, it differs from opinions, judgments, and evaluations, since they can only be partially verified.[78] Therefore, speculations and rumors cannot qualify as "information." Declarations of intention are treated in a similar fashion. As long as the impact of an event expressed in such a declaration depends on the occurrence of certain other events or the taking of further measures, the declaration does not constitute information, because it contains hypothetical situations.[79] In summary, "information" can be compared with the term "fact"[80] in the English language. Since the Act also speaks about *tatsache*, "facts," which is the more commonly known term, it will be used interchangeably with "information" in the following explanations.

To qualify as inside information, the information must be unknown to the public. It is not required, however, that it be treated as secret or confidential.[81] According to the explanation provided by the German legislature,[82] a fact is known to the public if knowledge of it is available to an unrestricted

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75. *Id.* § 18(1).
76. *Id.* § 38(2).
77. This is the official Federal Supervisory Authority translation of § 13(1). For the German text, *see supra* note 40 and accompanying text.
78. BT-DRUCKS, *supra* note 24, at 46; Immenga, *supra* note 5, at 201.
79. *See* ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 36.
80. *Tatsache* (fact).
81. SIEBOLD, *supra* note 5, at 232; Assmann, *The New German Insider Law*, *supra* note 5, at 510.
82. BT-DRUCKS, *supra* note 24, at 46.

number of people. More specifically, the German legislature regards a fact as publicly known if the market participants, for example, professional security traders or institutional investors, have the opportunity to take note of it.[83] This opportunity is more or less guaranteed if the facts are disseminated over information systems that are generally accessible throughout the investment community, such as widespread exchange newspapers, investment publications, and electronic news systems like Reuters.[84]

The reduction of the definition of "information" by the German legislature to the knowledge of market participants has not gone undisputed.[85] It seems problematical that the extent of the knowledge possessed by the broad spectrum of potential market investors appears to be unimportant to the German legislature's definition of what constitutes publicly known information, especially in light of the fact that the Securities Trading Act was designed specifically to protect and encourage this group. Therefore, the German legislature's decision results in a basis of informational knowledge between the broad investor group and the market participants that is as uneven as the disparity in information that exists between insiders and other investors. Some commentators thus propose that a fact is not publicly known until it has been published in the mass media and therefore, becomes available to the general public.

It should be noted, however, that the notification of a broad investor group can be achieved only through the use of mass media such as daily newspapers. Consequently, a relevant fact could remain unknown for a period of at least twenty-four hours. However, investors who rely on weekly investment magazines still would not be informed. Thus, the time lapse between the dissemination of insider information and its actual publication, making it available to the general public, would be at least one day and perhaps as long as one week. Such a situation leaves the possibility of either insider activities or trading restrictions on the persons involved during the interval between dissemination and publication.

By reason of legal certainty and practicability, the decision of the German legislature tends to be tenable. Indeed, the notification of market participants is suitable for immediately regulating the market price of securities and for avoiding insider trading. Consequently, the informational requirement focusing on the market participants is sufficient to achieve the objectives of the Act and to protect a broad spectrum of investors. Furthermore, most investors in German exchanges are represented by market

83. This refers to the *Bereichsöffentlichkeit* (sector publicity). BT-DRUCKS, *supra* note 24, at 46; Immenga, *supra* note 5, at 202.

84. ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 43; Caspari, *supra* note 5, at 539.

85. For more details about this discussion, *see* Assmann, *Part II*, *supra* note 5, at 241.

participants and therefore would benefit at least indirectly.[86]

Facts reported and published in compliance with the Act ease the inside information qualification. However, this provision of the Act is not immediately satisfied upon communicating the information to reporters, analysts, or information system providers. Rather, information does not qualify as publicly known until these people, in turn, transmit the information to the market participants.[87]

Another requirement for the term "inside information" is the relation of a fact to the issuer(s) of insider securities or to the insider securities themselves. Facts that relate to one or more issuers may thereby have their origin within or beyond the sphere of such issuers.[88] According to the Federal government's explanation[89] to the Act, facts within the sphere of an issuer include events such as the conclusion of important corporation contracts,[90] a new invention, or a capital reduction decision. A circumstance beyond the issuer's sphere might be a federal sale prohibition on one of the issuer's produced goods.[91]

Facts that relate to insider securities with respect to the price of such securities include: the knowledge of a forthcoming, large stock disposition and the buy/sell recommendations of analysts.[92] Market information also is covered under this criterion.[93] Market information can be defined as information dealing with the condition of markets as a whole, not only with regard to certain securities that obliquely affect the price of securities.[94] A decision of the Federal Bank[95] about the official discount rate,[96] natural disasters like thunderstorms over grain-growing regions, or political occurrences, such as the results of elections, can be considered market information and eventually inside information.[97]

Finally, an inside fact must have the potential to materially affect the price of insider securities. The German legislature enacted this requirement

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86. DEUTSCHE BÖRSE AG, *supra* note 5, at 18; Assmann, *Part II*, *supra* note 5, at 241; Caspari, *supra* note 5, at 539; Immenga, *supra* note 5, at 202.

87. ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 45; BECKER, *supra* note 5, at 64.

88. Kümpel, *supra* note 5, at n.14.104; Peltzer, *supra* note 5, at 749.

89. BT-DRUCKS, *supra* note 24, at 46.

90. The explanation explicitly mentions direct control contracts and agreements for the transfer of profits. *Id.*

91. *See* ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 50; DEUTSCHE BÖRSE AG, *supra* note 5, at 17.

92. Caspari, *supra* note 5, at 540; Claussen, *supra* note 5, at 29-30; Schwarze, *supra* note 5, at 134; Tippach, *supra* note 5, at 1270.

93. BECKER, *supra* note 5, at 65; Assmann, *The New German Insider Law*, *supra* note 5, at 513; Weber, *The New German Insider Law*, *supra* note 5, at 163.

94. Assmann, *Part II*, *supra* note 5, at 243; Immenga, *supra* note 5, at 202.

95. *Bundesbank* (Federal Bank).

96. *Diskontsatz* (official discount rate).

97. A more extensive list can be found in Tippach, *supra* note 5, at 1270.

with the purpose of excluding minor occurrences. Consequently, facts whose potential impact on the price of securities is minute will not be treated as inside information, even though they may meet the previously described standards.[98] As clarified by the legislature, the adequately determined possibility of influencing the price of insider securities satisfies this requirement of the term "inside information."[99] Whether a possibility has been adequately determined must be evaluated from an objective and forward-looking point of view. It is not the subjective evaluation of the person who has knowledge of such facts that is critical for this requirement. Rather, the possibility that the fact will materially affect the price must be foreseeable from the prospective of a reasonable third person.[100] What is not relevant is whether the price of an insider security actually changes after the facts have become known because the insider trading prohibition is a strict liability tort,[101] which punishes based on the possibility of the occurrence of certain events.[102]

In question is when can a "material" effect on price be assumed, since the Act itself does not contain a specific threshold. The legislature, however, in its explanation refers indirectly[103] to a provision contained in Section 8(1) of the "Conditions for Deals Concluded at German Securities Exchanges,"[104] where, for example, the materiality threshold for stocks would be five percent.[105]

Scholarly publications, for the most part, support the German legislature's proposal regarding the thresholds of the Act for determining what is "material."[106] Some authors propose alterations in the price of two percent[107] and some propose alterations of ten percent[108] (equal to a

98. BT-DRUCKS, *supra* note 24, at 46.

99. DEUTSCHE BÖRSE AG, *supra* note 5, at 20; *see* Weber, *The New German Insider Law*, *supra* note 5, at 163 (discussing how significant a piece of information must be in order to qualify as inside information).

100. For a more comprehensive explanation, *see* DEUTSCHE BÖRSE AG, *supra* note 5, at 18.

101. *Gefährdungsdelikt* (strict liability tort).

102. Weber, *The New German Insider Law*, *supra* note 5, at 163.

103. *Compare* explanation to the Act, BT-DRUCKS, *supra* note 24, at 47.

104. *Bedingungen für Geschäfte an den deutschen Wertpapierbörsen* § 8(1), KMR [hereinafter *Geschäftsbedingungen*] (This is a set of rules issued by a self-regulating body that regulates the course of business and which can be compared to the AMEX or NYSE.).

105. According to the *Geschäftsbedingungen*, *supra* note 104, § 8(1), brokers are obliged to announce expected stock price changes of more than 5% that result from high trading orders, with a single Plus or Minus notification. *Id.* For other securities, the threshold is different. By explicitly mentioning a single Plus or Minus notification as a material price alteration, the Federal government makes clear that it views the thresholds of § 8(1) as useful guidelines. *Id.*

106. *See, e.g.*, Assmann, *Part II*, *supra* note 5, at 244; Möller, *supra* note 5, at 106; SIEBOLD, *supra* note 5, at 233-34.

107. *See* BECKER, *supra* note 5, at 66.

double-plus or double-minus notification) as "material," without, however, convincingly explaining their reasoning. Still others generally object to the adoption of strict figures and prefer a case-by-case evaluation, since such numbers do not take into account the specific circumstances of each case.[109]

The figures of the *Geschäftsbedingungen*[110] are a useful instrument for determining specific thresholds for the term "material" because both the *Geschäftsbedingungen* and the Securities Trading Act share the same objective, namely to protect the equal chances of market participants by establishing market transparency.[111] Therefore, the single-plus or single-minus notification of the *Geschäftsbedingungen* should be chosen as the lowest thresholds, since there is no convincing reason why a huge trade order, which undoubtedly qualifies as inside information, should be subject to different thresholds specified in the two laws even though the laws have the same intention. Furthermore, despite the fact that a case-by-case evaluation admittedly would be the fairest solution, such a proposal must be rejected by reason of legal certainty that must provide a potential insider with a nominal definition of the term "material."[112] Therefore, in stock cases, this would mean that a material effect on price would be possible with a five percent alteration.

The determination of what inside information potentially will cause a single-plus or-minus price variation still has to be done by each potential insider. Although it is generally acknowledged that certain transactions possess a potential to cause a price change, ultimately, it depends on each individual case whether the information qualifies as information that may materially affect the price.[113] For instance, the conclusion of merger or acquisitions agreements, the purchase or sale of divisions, important inventions, product liability suits, changes in equity balance positions, as well as changes in the earnings expectations of enterprises, might have such a potential,[114] but the impact of each of these circumstances depends on the size of the involved corporation. In summary, potential insiders have to rely on their previous trade experience or the advice of their counselors, since

108. *See, e.g.,* Claussen, *supra* note 5, at 30.
109. *See, e.g.,* Peltzer, *supra* note 5, at 749; KÜMPEL, *supra* note 5, at n.14.128.
110. *See supra* note 105 and accompanying text.
111. *Compare* Immenga, *supra* note 5, at 203.
112. ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 69; Jander & Zoberbier, *supra* note 5, at 808.
113. DEUTSCHE BÖRSE AG, *supra* note 5, at 19; Weber, *The New German Insider Law*, *supra* note 5, at 164.
114. For a more comprehensive listing, *see* DEUTSCHE BÖRSE AG, *supra* note 5, at 26.

guidelines[115] have not yet been developed.

Section 13(2) of the Act limits the coverage of the above defined term "insider information." Accordingly, assessments that are compiled exclusively on information known to the public will not be deemed inside information, even if such assessments might materially alter the price of insider securities. This part is especially important for security analysts and business journalists, since the Act provides a safe harbor for their recommendations and analyses as long they only use information available to all market participants.[116]

Similar to the German Securities Trading Act, "inside information" is defined as material nonpublic information in U.S. laws.[117] The determination of materiality is not done with the use of strict thresholds, as have been proposed for the German Act, but by the application of the materiality standard expressed in *SEC v. Texas Gulf Sulphur Co.*[118] Under this standard, a fact is material if its disclosure is likely to cause a substantial change in the price of a security and if a " 'reasonable man would attach importance [to this fact] . . . in determing his choice of action.' "[119] While this definition is congruent with the German statutory language, a difference exists in the approach towards the final determination of materiality. Instead of using generally acceptable thresholds, an evaluation based on a case-to-case method is preferred in the United States.[120] The U.S. approach towards the existence of the *possibility* of a material price alteration resembles the discussion in the German Act.

In the United States, the definition of "nonpublic" information is, as it is in Germany, based on the efficient capital market hypothesis.[121] Thus, disclosure to "market participants," that is, publication available to marketplace traders instead of to a broad spectrum of investors, renders a fact publicly known.[122] In summary, the German legislature seems to have absorbed most of the experiences in the United States with regard to the

115. A possible guideline would be a chart, based on an empirical evaluation, that lists the potential implications of certain events on enterprises within different ranges of sizes, assets, shares, and so on.

116. *Compare* Assmann, *Part II*, *supra* note 5, at 244, *with* Möller, *supra* note 5, at 106.

117. Chiarella v. United States, 445 U.S. 222, 226-29 (1980); SEC v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1306 (2d Cir. 1971); SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 847 (2d Cir. 1968).

118. 401 F.2d at 848.

119. *Id.* at 849 (quoting List v. Fashion Park, Inc., 340 F.2d 457, 462 (2d Cir. 1965) (citations omitted).

120. *See, e.g.*, Goldman v. Belden, 754 F.2d 1059, 1060 (2d Cir. 1985).

121. 15 U.S.C.A. § 78j (1996).

122. *See* United States v. Libera, 989 F.2d 596, 601 (2d Cir. 1993); Elkind v. Liggett & Myers, Inc., 635 F.2d 155 (2d Cir. 1980), consistent with *Texas Gulf Sulphur*, 401 F.2d at 833.

definition of inside information. A minor difference exists only in the approach towards the determination of materiality. Whereas the German legislature obviously prefers the application of certain thresholds, the United States has adopted a more case-by-case evaluation.

2. Insider

The term "insider" restricts the personal applicability of the insider trading prohibition. The broad formulation of Section 13 of the German Securities Trading Act, however, qualifies every person or legal entity that has knowledge of inside information as an insider.[123] The underlying principle of Section 13 is the terminological differentiation between primary insider, referred to only as "insider" in the statutory language, and secondary insider, for which the Act in Section 14 uses the term "any third person." This distinction becomes important for the concrete restrictions of the insider trading prohibition.[124]

a. *Primary*

The term primary insider is distilled further in Section 13 of the Act as persons who are primary insiders (1) by reason of their integrated intercompany relationship to the issuer of insider securities,[125] (2) by reason of their participation in the share capital of an issuer,[126] or (3) by virtue of their profession or their activity with the issuer.[127] All of these groups also must know facts that objectively qualify as inside information. It is not required, however, that they actually recognize the inside information "quality" of the fact in their possession.[128]

Although insider trading law in the United States does not recognize a different statutory scheme for the three primary insider groups, it is widely recognized that primary insiders[129] can only be persons who (1) have traded in securities of a company (2) with which they stood in a fiduciary relationship, (3) while in possession of inside information.[130] The deter-

123. BECKER, *supra* note 5, at 58; Assmann, *The New German Insider Law*, *supra* note 5, at 504.

124. *See infra* part III.B.4.

125. WpHG § 13(1)1., v.26.7.1994 (BGBl. I S.1753).

126. *Id.* § 13(1)2., at S.1753.

127. *Id.* § 13(1)3., at S.1753.

128. *Compare* BECKER, *supra* note 5, at 59.

129. The term "primary insider" as found in the German Insider Law is the equivalent to insiders who stand in a fiduciary relationship with the issuer of insider securities in the U.S. insider terminology. For reasons of clarification, the German term also will be used in the following discussion of U.S. insider law.

130. DONALD C. LANGEVOORT, INSIDER TRADING: REGULATION, ENFORCEMENT & PREVENTION § 3.02, at 3-2 (Clark Boardmann Callaghan Securities Law Series, Rel. #3 7/94

mination as to whether a person owes a fiduciary obligation to the corporation in whose securities he traded is not always a clear one. However, nearly all of the groups mentioned in the German Act also could qualify as fiduciaries of such a corporation under U.S. law. Thus, the coverage of both laws is almost the same with respect to primary insiders. Some minor differences are noted in the discussion below.

According to WpHG Section 13(1)1., a primary insider is a person who as a member of the supervisory body[131] or management body,[132] or as a general partner[133] of the issuer or an enterprise associated with the issuer,[134] save knowledge of inside information. The issuer's or enterprise's organizational form is thereby irrelevant.[135] The only crucial factor is the issuance of insider securities or association with such an enterprise.[136] This category also is covered by the primary insider term under U.S. insider trading law.[137]

In question is whether a causal connection between the acquaintance with the inside information and the membership in such an issuer's body must exist. Some commentators assume that the formulation "an insider is anyone who *as* a member" was intended to cover only those persons who become familiar with inside information *because of* their membership.[138] The prevailing opinion, however, is that the language only requires the knowledge of inside information, regardless of whether it was gained by sitting on such a body or elsewhere.[139]

The latter, prevailing doctrine should be approved. First, the legislature has not implemented a causal connection requirement for this group, as it did in Section 13(1)2.-3. In the latter sections, the German legislature expressly decided to use the language "by virtue of" as such a requirement. By omitting a similar expression in Section 13(1)1., it can be assumed that it was the intention of the legislature not to require a causal connection for the members of issuer's body and general partners.

1994). This is based on the landmark decision of the U.S. Supreme Court in *Chiarella v. United States*, 445 U.S. 222 (1980).

131. *Aufsichtsrat* (supervisory body).

132. *Vorstand* (management body).

133. *Persönlich haftender Gesellschafter* (general partner).

134. *Verbundenes Unternehmen* (enterprise associated with the issuer).

135. They may be organized as corporations, limited liability companies, or limited partnerships, for example.

136. DEUTSCHE BÖRSE AG, *supra* note 5, at 7; Assmann, *The New German Insider Law*, *supra* note 5, at 505.

137. 15 U.S.C. § 78p (1994).

138. *Accord* Weber, *The New German Insider Law*, *supra* note 5, at 159.

139. DEUTSCHE BÖRSE AG, *supra* note 5, at 7; SIEBOLD, *supra* note 5, at 236-37; Claussen, *The New Insider Law*, *supra* note 5, at 27. Only the purely private acquisition of inside information is excluded. SIEBOLD, *supra* note 5, at 237.

Moreover, nearly all other countries with insider regulations have not implemented a causal connection clause for such persons. Since the German legislature wanted to achieve an internationally acceptable standard with its insider prohibition, it would have been in conflict with this purpose to construe such a requirement for a group that naturally deals with inside information on a daily basis. Rather, it can be concluded from the Federal government's explanation that even the slightest chance of insider dealing by this group was to be avoided by qualifying them, based upon the knowledge of inside information, as primary insiders.[140] In summary, the mere knowledge of inside information automatically qualifies the members covered under Section 13(1)1. as primary insiders.[141] In contrast thereto, in the United States it seems to be recognized that such a causal link is required for mandating the primary insider restriction on such persons.[142] Thus, despite the fact that such persons would be subsumed under the primary insider term in the United States, they would not be foreclosed from trading upon knowledge gained outside their fiduciary position.

According to Section 13(1)2., primary insiders also include participants in the share capital of the issuer or of an enterprise associated with the issuer. A necessary prerequisite is that the capital participation was the cause of their obtaining inside information.[143] A certain threshold of share participation is not required. Therefore, small shareholders of large, publicly traded corporations may be considered as primary insiders.[144]

Some object to this proposition, arguing that the legislature should have adopted a threshold for the protection of small shareholders.[145] Such a proposal can be rejected on the ground that the legislature introduced a causal requirement through the formulation "by virtue of," which in most cases that involve small shareholders will not be at hand. Should the small shareholders, however, satisfy the requirement, no convincing argument can be made why they should not be subject to the insider restrictions, since the element of injustice in insider transactions, namely the intentional exploitation of inside information, is present in insider trades of both minority and majority shareholders.[146] Conversely, U.S. insider trading law assumes that only controlling shareholders qualify as primary insiders

140. *See* BT-DRUCKS, *supra* note 5, at 46.
141. *See supra* notes 31-34 and accompanying text.
142. *See* LANGEVOORT, *supra* note 130, § 3.02, at 3-7, for further sources.
143. *Compare* Claussen, *supra* note 5, at 27, *and* Weber, *The New German Insider Law*, *supra* note 5, at 159.
144. Jander & Zoberbier, *supra* note 5, at 807; DEUTSCHE BÖRSE AG, *supra* note 5, at 7.
145. *Accord* Claussen, *supra* note 5, at 27.
146. *Accord* Assmann, *Part II*, *supra* note 5, at 239; Immenga, *supra* note 5, at 200; Jander & Zoberbier, *supra* note 5, at 807.

because only such persons are fiduciaries of a corporation.[147] Noncontrolling stockholders are not in a fiduciary relationship with the corporation and thus, are not subject to this term.[148] Consequently, they are only subject to restrictions applicable to them as tippees.[149]

Under the definition of Section 13(1)3. of the Act, persons who receive knowledge of inside information in due course of their profession, activity, or assignment also are covered under the primary insider term. The Federal government's explanation mentions as potential primary insiders certified public accountants, tax and business consultants, lawyers, and all employees of like professions.[150] With respect to the professionals listed in Section 13(1)3., the legislature enacted a double-causal connection requirement. First, they have to achieve knowledge of inside facts *by virtue of* their occupation. Second, they additionally must be privy to the information *in due course*. The latter restriction is of special importance, since it exempts the accidental acquisition of inside information from qualification as a primary insider. Consequently, a cab driver who coincidentally hears inside information in the conversation of his passengers would not become a primary insider. Even though he obtained the inside information by virtue of his profession, he did not do so in the due course of his employment. Furthermore, in contrast to situations covered under Sections 13(1)1.-2., the group under discussion does not have to stay in any kind of relationship with the issuer.[151] Nonetheless, some commentators assume that primary insiders as defined under Section 13(1)3. can only be persons who have a contractual relationship with the issuer. This point of view, however, is not convincing. First, such a restriction would conflict with the statutory formulation that provides for "by virtue of" and "in due course" requirements, but not for a "contractual relation" provision. Second, this definition of primary insider would not conform with Article 2(1), number 3 of the EU Directive on Insider Dealing.[152] Finally, there is no reason why employees of federal agencies like the Federal Cartel Office, who unquestionably have

147. *See In Re* Cady, Roberts & Co., 60 S.E.C. 907, 911-12 (1961); Speed v. Transamerica Corp., 99 F. Supp. 808, 829 (D. Del. 1951).

148. *See Cady*, 60 S.E.C. at 911-12.

149. With regard to the requirements to be met for such a tippee liability, *see infra* part III.B.4.a. & *supra* note 255. The term "tippee" in U.S. insider law covers persons who are considered to be secondary insiders under German insider law if the tippee acquires knowledge of inside information. Otherwise, he can not qualify as a secondary insider under German Law.

150. For a qualification of additional professional groups, *see* BT-DRUCKS, *supra* note 5, at 46.

151. Assmann, *Part II*, *supra* note 5, at 239; Caspari, *supra* note 5, at 538; Hopt, *Legal Problems*, *supra* note 5, at 90-91.

152. *See* EU Directive 89/592, *supra* note 21, art. 2(1); Ruiz, *supra* note 21, at 236-37.

access to inside information with a tremendous potential to affect prices[153] but do not have a contractual relationship with the issuer, should be exempt from the insider trading prohibition.[154]

The following examples illustrate what might be considered to be more relevant groups who can be regarded as primary insiders under Section 13(1)3. Employees of the issuer or of an enterprise associated with the issuer, such as junior managers below the management level, qualify as primary insiders if they specifically and during their course of conduct as specified in the employment contract acquire knowledge of inside information. For example, a curious secretary who reads transcripts designated for her supervisor but not for herself cannot be regarded as a primary insider, since she did not receive the insider information in due course. However, if she receives the transcripts as addressed to her, the due course requirement and therewith the primary insider position could be met.[155] Therefore, under the German Securities Trading Act primary insiders may be managers, as well as temporary employees or summer associates, on the other hand, high-positioned lawyers in the legal department of the issuer may not be subject to the primary insider term. In summary, a case-to-case evaluation must be done, focusing on the responsibilities of each person and whether inside information was obtained in due course.[156] United States insider trading law applies almost the same analytical steps for employees of the issuer: if an employee gained his knowledge in the course of his employment, he will be treated as a primary insider.[157] Thus, both the German and the U.S. securities laws lead to the same result.[158]

The rules established under the German Act for those employed by the issuer also can be applied to the persons with no regular employment contract. Lawyers, tax consultants, and certified public accountants who have a mandate with the issuer may be classified as primary insiders (as well as their employees). The issue is again whether the issuer intentionally provided these persons with the inside information, and whether they gained this information during their professional work for the issuer. In the United States, they are treated as "temporary" primary insiders.[159] Similar to its German counterpart, under U.S. securities law, an agency-like relationship

153. For instance, if a merger or acquisition agreement of two companies has to be approved.

154. *Accord* Hopt, *Legal Problems*, *supra* note 5, at 91; Immenga, *supra* note 5, at 200.

155. ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 22; DEUTSCHE BÖRSE AG, *supra* note 5, at 8.

156. Assmann, *The New German Insider Law*, *supra* note 5, at 507.

157. United States v. Carpenter, 791 F.2d 1024, 1026 (2d Cir. 1986).

158. *See Texas Gulf Sulphur*, 401 F.2d at 848.

159. Dirks v. SEC, 463 U.S. 646, 655 (1983).

must exist in order to impose primary insider liability on such persons.[160]

An analyst or business journalist who receives an invitation to a factory inspection and then gains inside information during a conversation with an issuer might be considered to be a primary insider, since the information was gained during his assignment and in due course from the issuer.[161] Under U.S. law, someone in this situation would be considered a temporary primary insider, if he acquired the information in a forum where the issuer mandates a fiduciary duty on them to keep it confidential or conversely to immediately and widely publicize it.[162] However, these persons also must have expressly or impliedly agreed to the imposition of such a duty.[163]

Interestingly, relatives, family members, and close friends of primary insiders who receive inside information in due course cannot be qualified as primary insiders because the transfer of the information did not occur during a professional or assigned relationship. Despite the fact that the qualification of this group as primary insiders would be desirable,[164] the German legislature failed to include them, and they are only subject to the secondary insider restriction.[165]

Employees of public agencies or institutions also may meet the requirement of Section 13(1)3., even if they do not stand in any contractual relationship with the issuer.[166] Thus, employees of the Federal Statistical Office[167] reporting the most recent inflation rate, officials of the Federal Bank publishing the new official discount rate,[168] or investigators of the Federal Environmental Agency[169] filing reports about violations against Environmental Laws fulfill the requirements of Section 13(1)3.[170] This is equally true under U.S. law. Although such persons are not directly fiduciaries of the issuer or its shareholders, under the "public trust theory," they do owe a fiduciary duty to the broad investor spectrum, since an unjust

160. *See, e.g.*, SEC v. Tome, 638 F. Supp. 596 (S.D.N.Y. 1986). Whether the employees of such persons also can be treated as primary insiders in the United States is a difficult question since they receive the inside information not directly from the issuer, but from the person to whom the information was dedicated.

161. KÜMPEL, *supra* note 5, § 14.165; Assmann, *Part II*, *supra* note 5, at 239.

162. *Dirks*, 463 U.S. at 655.

163. *See* SEC v. Ingram, 694 F. Supp. 1437, 1440 (C.D. Cal. 1988).

164. It is desirable because of the frequency with which these people will receive insider facts and because different restrictions are applicable to primary and secondary insiders.

165. ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 26; Weber, *The New German Insider Law*, *supra* note 5, at 162.

166. *See supra* part III.B.2.

167. *Statischtisches Bundesamt* (Federal Statistical Office).

168. *Bundesbank* (Federal Bank), *Diskontsatz* (official discount rate).

169. *Bundesumweltamt* (Federal Environmental Agency).

170. *Compare* ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 28, *and* Immenga, *supra* note 5, at 201.

enrichment situation is present.[171] Hence, U.S. securities law comes to the same conclusion as the German insider law.

b. *Secondary*

With reference to Section 14(2) of the German Act, every third party who has knowledge of inside information and cannot be subordinated to one of the primary insider groups automatically assumes a secondary insider position. The actual circumstances under which such a person gained knowledge of inside information are not relevant. Accordingly, a person who is intentionally told the information by a primary insider qualifies as a secondary insider, as well as a cab driver or an industrial spy who discover the fact by secretive listening. Similar to the primary insider discussion, the secondary insider terminology of Section 14(2) only requires that the relevant fact constitute inside information from an objective point of view. A person who does not know that the information in his possession is "inside" in nature assumes a secondary insider position as well.[172] Persons receiving only a tip or buy/sell recommendation from insiders without any further explanation do not become secondary insiders because they did not acquire the insider information upon which the recommendation was founded.[173]

In summary, the broad scope of the statutory formulation of the secondary insider term functions as an "omnibus clause,"[174] intended to cover every person with knowledge of facts that objectively qualify as inside information. The doubtful extension of the secondary insider term to persons who unknowingly possess inside information is limited by the phrase "based on such knowledge," contained in the trading prohibition of Section 14(2).[175] This formulation indicates that a secondary insider must have knowledge about the quality of the used information in order to have violated the secondary insider restriction.[176] Under U.S. laws, the above mentioned group of secondary insiders are called "outsiders."[177] The extension of the insider obligation to such persons is not as easily available as it is under the German statutory formulation. Rather, in the United States, the misap-

171. *See* LANGEVOORT, *supra* note 130, § 3.02, at 3-14.

172. BECKER, *supra* note 5, at 62; Assmann, *The New German Insider Law*, *supra* note 5, at 508.

173. BECKER, *supra* note 5, at 63; Assmann, *Part II*, *supra* note 5, at 248; Immenga, *supra* note 5, at 201. The primary insider giving such a recommendation is, however, punishable under § 14(1)3.

174. *Auffangstatbestand* (omnibus clause).

175. DEUTSCHE BÖRSE AG, *supra* note 5, at 8; Weber, *The New German Insider Law*, *supra* note 5, at 162.

176. DEUTSCHE BÖRSE AG, *supra* note 5, at 8; Weber, *The New German Insider Law*, *supra* note 5, at 162.

177. *Dirks*, 463 U.S. at 655, 663.

propriation theory has to be employed to cover insider trading by persons who do not directly owe a fiduciary duty to the issuer of insider securities or its shareholders.[178] This theory thereby imposes SEA Section 10(b) and Rule 10b-5 liability on an individual who "(1) misappropriates material nonpublic information (2) by breaching a duty arising out of a relationship of trust and confidence and (3) uses that information in a securities transaction, (4) regardless of whether he owed any duties to the shareholder of the traded stock."[179]

3. Insider Securities

The legislature has defined in Section 12 of the German Securities Trading Act the scope of securities it intends to be protected by the insider trading prohibition. The Act's formulation covers securities and derivatives.

a. *Securities*

All securities that are in accordance with Section 2(1) of WpHG and are included or admitted to trading on a domestic market are automatically insider securities.[180] Referring to the statutory formulation of Section 2(1), these securities are, on the one hand shares,[181] certificates representing shares, debt securities,[182] participation rights[183] and warrants,[184] and on the other hand, securities comparable to shares or debt securities. The latter formulation includes securities reflecting a membership right in an association or federation.[185] All of these securities must be traded on a market that operates on a regular basis and is accessible, whether directly or indirectly,

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178. SEC v. Clark, 915 F.2d 439, 443 (9th Cir. 1990).

179. *Clark*, 915 F.2d at 443; United States v. Bryan, 58 F.3d 933, 944 (4th Cir. 1995); *see* 17 C.F.R. § 240.10b-5 (1998). The misappropriation theory is, however, not undisputed between the different U.S. Courts of Appeals. While the Second, Third, Seventh, and Ninth Circuits have adopted this theory, it was rejected in *United States v. O'Hagan*, 92 F.3d 612 (8th Cir. 1996), by the Eighth Circuit as not being protected by the clear language of Section 10 (b) of the SEA and the legislative history thereto. For a comprehensive discussion of the misappropriation theory, *see* David Cowan Bayne, *Insider Trading and the Misappropriation Theory: The Awakening, 1995*, 30 LOY. L.A. L. REV. 487 (1997). For a discussion of this theory after the recent *O'Hagan* decision, *see* Jonathan E.A. ten Oever, *Insider Trading and the Dual Role of Information*, 106 YALE L.J. 1325 (1997); Kathryn Keneally, *Ins and Outs of Insider Trading*, 21 CHAMPION 25 (1997).

180. WpHG § 12(1)1., v.26.7.1994 (BGBl. I S.1753).

181. *Aktien* (shares). Thereunder fall shares made out to the holder as well as registered shares and not freely transferable registered shares.

182. *Schuldverschreibungen* (debt securities). They might be issued by either the government or enterprises.

183. *Genußrechte* (participation rights).

184. *Optionsscheine* (warrants)

185. *Verband* (federation, association). *See* ASSMANN & SCHNEIDER, *supra* note 5, § 2 para. 6; SIEBOLD, *supra* note 5, at 224.

by the public.[186] By this definition, for example, all securities that are either admitted to German exchanges for the official listing[187] or the regulated listing,[188] or included in the over-the-counter market[189] are covered under the insider securities term.

Through Section 12(1) sentence 2, securities for which an application for admission or inclusion has been made or publicly announced become subject to trading restrictions as insider securities.[190] An application is deemed to have been made if the competent exchange receives it. The public announcement requirement is satisfied by the availability of the information to the market participants.[191] Furthermore, insider securities are securities that are admitted to trading in another Member State of the European Community or another Contracting State of the Agreement on the European Economic Area,[192] subject to the market definition of Section 2(1) and to Section 12(1) sentence 2.

The ability to punish insider trading in preferred or common registered stock also is easily at hand under U.S. laws, since it is exactly this group of the issuer's shareholders to whom the fiduciary obligation is owed. In the case of debt securities, the situation is different. This contrariety can be explained by the fact that it is arguable whether the insider's fiduciary obligation also protects debt securities holders. Consequently, while the German Act avoids such problems by explicitly including debt securities in the insider securities term, U.S. laws probably have to apply the misappropriation theory to reach similar results.[193]

b. *Derivatives*

In addition to securities, derivatives are included in the insider securities term.[194] However, the definition of "derivatives" in Section 12(2) and Section 2(2) is not exactly the same as that of "securities." In contrast to Section 2(2), all three categories of Section 12(2) mandate a relation of the

186. *Compare* the explanation of the Federal government, BT-DRUCKS, *supra* note 24, at 39.

187. Änderung des Börsengesetzes (Stock Exchange Act) [hereinafter BörsenG], § 36, *as amended by* Zweites Finanzmarktförderungsgesetz, art. 2., v.26.7.1994 (BGBl. I S.1760). *Amtlicher Handel* translates as "official listing." *Id.* The original Stock Exchange Act was enacted in June 22, 1896.

188. *Id.* § 73 (*Geregelter Handel*).

189. *Id.* § 78 (*Freiverkehr*).

190. ASSMANN & SCHNEIDER, *supra* note 5, § 12 para. 3; Caspari, *supra* note 5, at 534.

191. BT-DRUCKS, *supra* note 5, at 45.

192. *Id.*

193. United States insider law reaches the same outcome with the application of the misappropriation theory, which was briefly discussed at *supra* note 167. For a discussion of this problem and a detailed citation list, *see* LANGEVOORT, *supra* note 130, § 3.03, at 3-18.

194. WpHG § 12(2), v.26.7.1994 (BGBl. I S.1753).

derivatives of the former provision with securities.[195] Therefore, derivatives priced on the alteration of foreign currencies or discount rates are not considered insider securities, because the basis for securities is lacking.[196]

Covered under the derivative term are rights to the subscription, purchase, or sale of securities.[197] This can be the subscription right for issuance of shares.[198] Put/call options also are contained under this sentence. Moreover, rights entitling the holder to a payment of an amount calculated on the basis of the performance of a securities basket are part of the definition.[199] In addition, financial futures,[200] that is to say future contracts[201] relating to a share or bond index or interest futures contracts,[202] as well as rights for the subscription, purchase, or sale of financial futures, are considered insider securities, provided that the subject of such financial futures is securities or financial futures related to an index that includes securities.[203] Pursuant to Section 12(2)4., futures contracts that provide a duty to purchase or sell securities are insider securities.[204] These contracts, in contrast to put/call options, not only entitle but also oblige the holder to purchase or sell specific securities.[205]

All the derivatives of Section 12(2), as well as the securities on which the derivatives are based, must be admitted or included in a domestic market as described above. An application for admittance or inclusion satisfies this prerequisite, whereby a market, as defined in Section 2(1), of a Member State of the European Community or another Contracting State of the Agreement on the European Economic Area is equal to a German market. It is not required, though, that both the derivative and the security be admitted in one and the same country.[206] In the United States, insider trading in options is prohibited by Section 20(d) of the SEA.[207] Thus, the German and U.S. acts both arrive at the same result, although the U.S. approach causes some conceptual problems with the requirement of an existing fiduciary duty

195. ASSMANN & SCHNEIDER, *supra* note 5, § 12 para. 8; BECKER, *supra* note 5, at 69.
196. *Compare* Caspari, *supra* note 5, at 534.
197. WpHG § 12(2)1., v.26.7.1994 (BGBl. I S.1753).
198. *Aktienemission* (issuance of shares). BT-DRUCKS, *supra* note 24, at 45.
199. WpHG § 12(2)2., v.26.7.1994 (BGBl. I S.1753). For a more comprehensive discussion, *see* BECKER, *supra* note 5, at 70; BT-DRUCKS, *supra* note 24, at 45.
200. *Finanzterminkontrakte* (financial futures).
201. *Terminkontrakte* (future contracts).
202. *Zinsterminkontrakte* (interest futures contracts).
203. WpHG § 12(2)3., v.26.7.1994 (BGBl. I S.1753).
204. *Id.* § 12(2)4.
205. *Id.* As an example, the bond-future contract traded at the *Deutsche Termin Börse* (German Futures Exchange) falls under § 14(2)4.
206. *Compare* Caspari, *supra* note 5, at 536.
207. 15 U.S.C. § 78t(d).

between the seller of the option and the insider.[208]

4. Prohibition of Insider Dealing

The insider trading prohibition is formulated in Section 14 of WpHG. The prohibition regulation of this provision differentiates between primary[209] and secondary insiders.[210]

a. *Pertaining to Primary Insiders*

Pursuant to Section 14(1), a primary insider, based on his knowledge of inside information, may not purchase or sell insider securities "for [his] own account or for the account or on behalf of a third party."[211] In addition, a primary insider may not make this information available to another person without authorization.[212] Finally, a primary insider is prohibited from recommending trades in insider securities to another person if the recommendation is based on inside information.[213] The phrase "for [his] own account or for the account . . . of a third party"[214] of the statutory formulation refers to transactions in which the primary insider makes his own investment decisions for his account or the account of one of his customers. The phrase "on behalf of a third party" refers to trades in which the primary insider executes orders as an agent of a third person. This might be, for example, the employer of the primary insider.[215]

It is important to note that the criterion "to purchase" or "to sell" only covers judicial acts in the form of an active transaction. "Nonselling" or "nonpurchasing decisions," however, are not included under these restrictions. This leads to the unsatisfactory situation where a primary insider who, after receiving inside information that security *X's* price will rise because of certain specified circumstances, decides not to sell his *X* security, does not violate the insider trading prohibition, even though prior to receiving the inside information he had intended to sell security *X*.

This gap in the provision has been widely criticized, since both the nonperformance and performance of an act, based on the knowledge of inside

208. The seller of options is not necessarily a shareholder of the issuer of the underlying security. Hence, the insider does not always owe a fiduciary duty to such seller.
209. WpHG § 14(1), v.26.7.1994 (BGBl. I S.1753) (described as "insiders").
210. *Id.* § 14(2), at S.1753 (described as "any third person").
211. *Id.* § 14(1)1., at S.1753.
212. *Id.* § 14(1)2., at S.1753.
213. *Id.* § 14(1)3., at S.1753.
214. *Id.* § 14(1)1., at S.1753.
215. ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 14; BECKER, *supra* note 5, at 49.

information, contain the same element of inequity.[216] It is recognized, however, that even if the Securities Trading Act had contained such a provision, in practice, it would have been impossible for prosecutors to produce sufficient evidence to satisfy their burden of proof. For this reason, despite the fact that it would have been sound from a theoretical point of view to include a provision covering nonselling or nonpurchasing, the Act's limitation to affirmative acts seems justifiable.[217]

Of decisive significance is the meaning of the phrase "on the basis of [his] knowledge of inside information"[218] as the subjective element of the insider trading prohibition, since only the presence of both the subjective and the objective part[219] finally leads to a punishable violation of the insider trading restriction. The exact definition of this subjective requirement is unfortunately not enunciated in the Act. The legislature nevertheless expressed its opinion in its explanation of the Act.[220] Pursuant to it, the requirement "on the basis of [his] knowledge" should be affirmed if the primary insider uses the information to the advantage of himself or others with the hope and goal of gaining an economic benefit, which commonly would be despised as a moral infringement of the equal opportunities for all investors. Hence, this provision requires that a deliberate, economic benefit be possible from the use of inside information.[221] In other words, the primary insider first must have the knowledge that he actually used inside information. Second, he must have the intent of utilizing this inside information for his own or a third party's benefit.[222] However, it is not required that the primary insider actually gain economic advantage from the insider transactions.[223]

In summary, a primary insider must possess intent with regard to all elements of the insider trading prohibition. Therefore, a primary insider who wrongly assumes that the inside facts do not meet the Act's criteria on affecting price or who assumes that the facts are already publicly known is not committing a violation of the insider trading restriction when he

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216. *Accord* Claussen, *supra* note 5, at 31; Hopt, *European & German Insider Law*, *supra* note 5, at 45.

217. BECKER, *supra* note 5, at 50; Assmann, *Part II*, *supra* note 5, at 246. Likewise, § 14(1)2.-3. does not cover the nonperformance of the therein described actions. Such an omission can be explained, however, with the same reasons as given for § 14(1)1.

218. WpHG § 14(1)3., v.26.7.1994 (BGBl. I S.1753).

219. The objective part is the occurrence of transactions in insider securities. In § 14(1)2.-3., the objective part is the disclosure of inside information to others, respectively the recommendation of transactions to third persons. *Id.* § 14(1)2.-3.

220. *Compare* BT-DRUCKS, *supra* note 5, at 47.

221. Immenga, *supra* note 5, at 204; Jander & Zoberbier, *supra* note 5, at 808.

222. Claussen, *supra* note 5, at 31.

223. Assmann, *Part II*, *supra* note 5, at 246; Jander & Zoberbier, *supra* note 5, at 808.

concludes transactions in insider securities based on his knowledge.[224] The statute expressly mentions that acting on one's own entrepreneurial decisions, even if founded on special knowledge, does not violate Section 14, as long as the decision was not influenced by otherwise, unlawfully accumulated insider facts.[225]

A primary insider will generally fall under an abstention or disclosure duty under U.S. insider laws.[226] Thus, insider trading by which the insider attempts benefit his own account or the account of others automatically leads to an insider violation.[227] What is arguable is the motivation that is necessary for a primary insider to be considered to have committed unlawful conduct, or to put it into the language of the German Act, whether the primary insider must have conducted a trade based on his knowledge of inside information. In the United States, the law is unclear with respect to this question. However, the statutory formulation chosen in Section 21A(a)(1) of the SEA seems to indicate that the mere possession of inside information invokes the abstention rule, without requiring an additional causal requirement,[228] as is contained in the German Act. Interestingly, the U.S. law faces the same problem as its German counterpart in the case of nontrading based on the knowledge of inside information. Hence, a director who changes his previous intention to sell stock after learning that his corporation's performance was better than expected cannot be punished under either German or U.S. insider law.[229]

As mentioned previously, official exchange brokers can be regarded as a professional group who typically would qualify as primary insiders, since they are confronted regularly with orders that might be determined as inside information. Their qualification as a primary insider is therefore not problematic. More important is the question of which broker deals will trigger the insider trading prohibition, because a primary insider can still conclude securities transactions as long as he does not make use of his insider knowledge. Hence, if an exchange broker is consulted regarding a plain order to buy stock from corporation *X*, he does not violate the insider

224. Since the Securities Trading Act does not regulate the negligent commission of an insider restriction violation, the primary insider in the illustrated example cannot be punished under the Act. *See* ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 19 (discussing this point in detail).

225. *Compare* BT-DRUCKS, *supra* note 24, at 47. *Accord* SIEBOLD, *supra* note 5, at 240; Assmann, *Part II*, *supra* note 5, at 246; Caspari, *supra* note 5, at 542; Möller, *supra* note 5, at 106.

226. *Dirks*, 463 U.S. at 655 n.14.

227. *See, e.g.*, *Tome*, 638 F. Supp. at 596.

228. LANGEVOORT, *supra* note 130, § 3.04, at 3-22; 15 U.S.C. 78u-1(a)(1).

229. *See* Steven R. Salbu, *Tipper Credibility, Noninformational Tippee Trading, and Abstention from Trading: An Analysis of Gaps in the Insider Trading Laws*, 68 WASH. L. REV. 307, 333 (1993).

trading prohibition, even if he qualifies a primary insider, since the transaction is taking place without the use of inside information.[230]

However, if the exchange broker receives an order that allows him to make the final investment decision of when security *X* has to be purchased, and the broker has insider facts about this security, then he undoubtedly will commit a violation of the insider trading prohibition. Therefore, he has to return orders that require him to make his investment decisions based on inside information that he possesses about the security to be traded. Another point of view contends that the broker should be permitted to execute the order if he could have come to the same investment decision by having used his market experience rather than his insider knowledge.[231] This proposal should be rejected as impracticable, since it would be impossible to verify that the investment decision was not based, at least in part, on inside information. Similarly, the Federal government's solution whereby such a broker simply should pass on the order to a colleague is not viable for two reasons. First, the colleague to whom the order is passed also might be in possession of insider facts. Second, the transfer of an order would indicate to the colleague that relevant and unknown information exists about the security that might substantially affect its price. Thus, the transfer of the order would come very close to an infraction of Section 14.[232]

A classic example of insider trades covered by the insider trading restriction is front running. Front running exists if brokers or security dealers, confronted with voluminous and therefore price relevant dispositions of a certain security, make their own trades in the security prior to the execution of the order, thereby utilizing their inside knowledge about its disposition. In order for a violation of Section 14 to occur, the disposition must, of course, have the potential of altering the price.[233]

Section 14 does not apply to "scalping." Scalping applies to cases in which buy/sell recommendations are publicly announced, and the recommender, normally a business journalist or an analyst, deals in the recommended securities prior to the announcement in order to profit from an expected subsequent price alteration. Although scalping is ethically intolerable, it is not covered under the insider trading prohibition, since the recommender is merely realizing his own investment decision. The fact that he subsequently causes other persons to follow his advice does not convert his investment decision into inside information. Obviously, if the recommen-

230. This is the explanation of the Federal government as contained in BT-DRUCKS, *supra* note 24, at 47.

231. *Accord* Claussen, *supra* note 5, at 29.

232. *Accord* Weber, *The New German Insider Law*, *supra* note 5, at 161.

233. *Compare* Kümpel, *Inside Information*, *supra* note 5, at 2139, *and* BECKER, *supra* note 5, at 54.

dation were based on information available only to the recommender, he could be called to account under Section 14.[234]

Section 14(1)2. furthermore punishes the disclosure or the "making available" of inside information without permission. The term "making available" means passively providing facts to third persons. Hence, if the primary insider creates a situation under which a third party can acquire the insider facts, he fulfills the "making available" requirement of Section 14(1)2., even without having actively given the information to the third party.[235] The legislative explanation[236] to the Act gives as an example of "making available" the situation where a primary insider communicates a password to a third person by which the latter gains access to restricted data systems containing inside information. Of specific importance is under what circumstances a disclosure or accessibility is unauthorized within the statute's meaning, since it is only then that the primary insider commits unlawful conduct. The explanation to the Act states that unlawful disclosure or accessibility is deniable if the inside information was given or made available within the regular course of conduct required by the primary insider's profession or employment.[237] It has to be acknowledged, however, that not every transmission of such information made within the regular course of conduct can be regarded as permissible, since it is the Securities Trading Act's objective to keep the number of potential insiders as small as possible.[238] For this reason, only inside information transfers that are absolutely required from an operational or assignment-based point of view are in compliance with Section 14(1)2.[239] Therefore, enterprises are strongly encouraged to create "Chinese walls" to ensure that only those people for whom it is essential receive the insider information.[240] The transmission of inside information to persons outside the business or enterprise, for example, to lawyers, certified public accountants, or exchange officials, is permissible only if it is necessary because of a legal obligation or can be justified by compelling business reasons.[241] Moreover, only the actual possession by the third party of the insider facts made available to the third party constitutes the statutory definition of Section 14(1)2. Therefore, the primary insider does not commit a violation of the insider trading

234. *Compare* ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 34.
235. Immenga, *supra* note 5, at 204; Möller, *supra* note 5, at 107.
236. BT-DRUCKS, *supra* note 24, at 47.
237. *Id.*
238. *Compare* Assmann, *Part II*, *supra* note 5, at 247.
239. This is the prevailing opinion. *See* DEUTSCHE BÖRSE AG, *supra* note 5, at 11; Assmann, *Part II*, *supra* note 5, at 247; Immenga, *supra* note 5, at 204; Jander & Zoberbier, *supra* note 5, at 808.
240. *Compare* DEUTSCHE BÖRSE AG, *supra* note 5, at 11.
241. Assmann, *The New German Insider Law*, *supra* note 5, at 520.

prohibition if the third party does not receive the insider facts given to him or receives them incorrectly, or if the third party already has knowledge of such facts.[242] The intent of the primary insider has to cover the recognition of facts as inside information as well as the receipt of the inside information by a third person.[243]

An unlawful disclosure can occur during discussions or presentations of company representatives with journalists or analysts. In many cases, during these conversations, company representatives mention facts that are not publicly known. Thus, they will commit a legal offense if they do not expressly convey the inside information to the group of journalists and analysts with the obligation that they immediately publish the information.[244] In the event that the company representatives transfer this duty to the persons present, the latter are prohibited from concluding any transaction in the affected securities prior to the publication of the inside facts.[245]

With regard to shareholder meetings, commentators question whether the chief executive officer[246] or other members of the senior management board[247] of a corporation violate Section 14(1)2. if they comply with their duty under the Corporation Act to answer shareholder questions.[248] Such a violation could occur since the members of the management board qualify as primary insiders under Section 13(1)1., and the shareholders of the corporation would be the "other persons" of the unlawful disclosure provision of Section 14. Therefore, answering a shareholder question could constitute a violation of this provision if the response contained inside information. The response could not be treated as a permissible publication of inside information under Section 15 (ad-hoc publicity) because the shareholders present constitute only a restricted forum.[249] Consequently, members of the board would be forced to make use of their right not to respond[250] if the answer would commit a legal offense.

Hence, some commentators propose that responses of members of the

242. ASSMANN & SCHNEIDER, *supra* note 5, § 14 paras. 44-45. This can be explained by the fact that the attempt to commit the criminal offense of § 14 is not punishable.

243. *Id.* § 14 para. 67.

244. For more information, *see* DEUTSCHE BÖRSE AG, *supra* note 5, at 11.

245. The transaction renders them secondary insiders. *Compare* Schwarze, *supra* note 5, at 128.

246. *Vorstandsvorsitzende* (chief executive officer).

247. *Vorstand* (senior management board).

248. The members of the management body are forced under § 131 of the Corporation Act to answer questions of shareholders who invoke this provision. AktG § 131, v.6.9.1965 (BGBl. I S.1089-1185).

249. *See* Joussen, *supra* note 5, at 2486, for a more comprehensive illustration.

250. *Auskunftsverweigerungsrecht* (right to reject to answer to a shareholder question) pursuant to AktG § 131(3) & (5), v.6.9.1965 (BGBl. I S.1089-1185).

management board to shareholder questions during a shareholder meeting should be treated as authorized and thus, not in violation of Section 14(1)2. because the goal of the Act is to protect shareholders by providing them with adequate information. For this reason, it would be contraobjective of the Act if shareholders could not receive answers to their questions because of a too narrow interpretation of the unlawful disclosure provision.[251] In accordance with another opinion, the management board's response would qualify as an illegal disclosure that could not be justified by the right of shareholders to pose questions and have them answered. Therefore, the members of the management would be entitled not to answer such questions in order to avoid criminal actions against themselves.[252]

Unquestionably, the Securities Trading Act attempts to accomplish effective shareholder protection. It is, however, not limited to the protection of shareholders of only one corporation. Rather, all shareholders and all potential investors have to be taken into account. Thus, if the disclosure of inside information during the shareholder meeting of corporation *X* is treated as legally permissible, all other investors who are not shareholders of *X*, as well as the shareholders of *X* not participating in the shareholder meeting, would be discriminated against. Furthermore, the informational rights of shareholders with regard to inside information are already satisfied through the ad-hoc publicity requirement under Section 15. Consequently, the second opinion, whereby management responses containing inside information would qualify as unauthorized and in violation of Section 14(1)2., should be given preference.[253]

Business journalists potentially could violate the unlawful disclosure provision. Undoubtedly, they are not in conflict with this regulation if they write articles recommending certain securities, and their recommendation is based on publicly[254] known facts. In the case where business journalists receive inside information, however, they must be aware that publication of this information is permissible only if the publication is made available to all market participants. Transmission of inside information to a restricted group of people constitutes a legal offense pursuant to Section 14(1)2.-3.

In the United States, liability for unlawful disclosure by primary insiders arises, for example, out of tipper-tippee liability. In the United States, a tippee violates insider laws if (1) the insider gives the tippee inside information, and the insider therewith seeks to benefit personally, and (2) the

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251. *See* Benner-Heinacher, *supra* note 5, at 766 (supporting this view).

252. *See* Joussen, *supra* note 5, at 2489; Kümpel, *Inside Information*, *supra* note 5, at 2138.

253. For discussions reaching the same result, but with minor differences in the analytical steps leading to it, *see* ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 51; Joussen, *supra* note 5, at 2486; Kümpel, *Inside Information*, *supra* note 5, at 2138.

254. "Publicly" is defined as publicly known to the market participants.

insider thus breaches his fiduciary loyalty to the issuer, with (3) the tippee's actual or constructive knowledge of the breach. If these conditions are met by the tippee, then both he and the primary insider automatically become subject to insider liability.[255] Furthermore, under U.S. law, in a tender offer context, Rule 14e-3 of the SEA prohibits the offering person, whether he is the issuer, or any officer, director, employee, advisor, or anybody else acting on behalf of the above mentioned group, from communicating material, nonpublic information relating to the tender offer.[256] A safe-harbor exemption exists for good faith communications required by law or for business purposes.[257]

Finally, under the German Act primary insiders also are excluded from recommending to another person the purchase or sale of insider securities if the recommendation is based on inside information.[258] The purpose of this regulation is to prevent evasion of the insider trading prohibition through the interaction between primary insiders and third persons.[259] The term "recommending" used in Section 14(1)3. of WpHG differs from "disclosure" as mentioned in Section 14(1)2. in the following respect: in a disclosure, the insider facts themselves are revealed to the third person, whereas a recommendation only provides a trading tip stating what or what not to do without actually disclosing the insider facts upon which the recommendation is grounded.[260]

The clear statutory formulation of Section 14(1)3. does not cover the dissuasion of third persons from making a previously intended transaction.[261] Thus, a primary insider does not violate this regulation if he gives a third person a hint not to execute an order that the third party had intended to execute before receiving the tip from the insider. The adoption of a clause prohibiting the dissuasive tip, however, appears to be necessary, since the Act as it stands clearly contains a regulatory leak that can and most likely will be exploited by savvy primary insiders and their customers. U.S. insider law is, in this respect, quite similar. Although the German Act distinguishes between the disclosure of inside information and the giving of a mere tip, U.S. law applies the tipper-tippee liability in both situations, with the result

255. *See Dirks*, 463 U.S. at 646 (stating the requirements for tipper-tippee liability).
256. 17 C.F.R. § 240.14e-3(d)(1)-(2) (1998).
257. *Id.* § 240.14e-3(d)(1)(i)-(iii). An example of such a business purpose is the communication of such information to persons involved in the planning or financing of the tender offer or in actions of the issuer in response to the tender offer.
258. WpHG § 240.14(1)3., v.26.7.1994 (BGBl. I S.1753).
259. Immenga, *supra* note 5, at 204; Jander & Zoberbier, *supra* note 5, at 808; Weber, *Changing Situation*, *supra* note 5, at 2853.
260. *Compare* DEUTSCHE BÖRSE AG, *supra* note 5, at 11.
261. ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 72.

being the same as that in Germany.[262]

By virtue of their profession, analysts usually face the danger of noncompliance with the prohibition of recommendations. Although recommendations pursuant to analyses of already known facts are protected,[263] the rendering of advice based on information revealed only to the analyst or a small group of analysts constitutes a violation of Section 14(1)3. Consequently, if an analyst receives new information about an enterprise during a presentation by the representatives of the enterprise, he then qualifies as a primary insider, since the disclosure occurred during the analyst's activity in due course. Consequently, he needs to be very careful about his future proceedings.[264] If he wants to utilize this newly gained information when making a recommendation, he must make sure that the new facts are first published and available to all market participants before releasing his advice.[265]

b. *Pertaining to Secondary Insiders*

According to Section 14(2) of the Act, a secondary insider is prohibited from purchasing or selling insider securities "for his own account or for the account of or on behalf of others[,]" as long as the transaction is grounded on inside information.[266] With regard to the definition of the various elements of this provision, this article refers to its previous explanations provided for primary insiders, since the meaning of the elements of both provisions is congruent.

Like primary insiders, secondary insiders must have intent with regard to all the requirements of Section 14(2).[267] Pursuant to this section, the ability to prosecute a secondary insider who receive inside information from primary insiders and subsequently conclude transactions in insider securities must be denied if the secondary insider has assumed in good faith that the insider facts were already publicly known. The fact that persons obtaining recommendations from primary insiders do not qualify as secondary insiders because they do not retain knowledge of insider facts themselves is important. Such persons are not legally excluded from utilizing the tip.[268] However, the primary insider who gives the recommendation is punishable

262. *Dirks*, 463 U.S. at 646.
263. WpHG § 13(2), v.26.7.1994 (BGBl. I S.1753).
264. This is the prevailing opinion. *See* ASSMANN & SCHNEIDER, *supra* note 5, § 13 para. 24; Caspari, *supra* note 5, at 538; Möller, *supra* note 5, at 104; Schwarze, *supra* note 5, at 128.
265. Caspari, *supra* note 5, at 538; Schwarze, *supra* note 5, at 128.
266. WpHG § 14(2), v.26.7.1994 (BGBl. I S.1753).
267. Assmann, *Part II*, *supra* note 5, at 248; Immenga, *supra* note 5, at 204.
268. *Compare* ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 74.

under Section 14(1)3. In addition, it is not necessary for secondary insiders to know which primary insider gave them the inside information, since the definition of the secondary insider term refers to the knowledge of the inside information itself.[269]

The prohibition regulation for secondary insiders does not contain a disclosure or recommendation restriction as is defined for primary insiders. Therefore, such a course of conduct cannot be prosecuted directly under the German insider law.[270] For this reason and in recognition of an otherwise existing regulatory leak, the German Federal Council,[271] during the enactment process of the Second Financial Market Promotion Act, proposed to amend the drafted insider law with a provision prohibiting disclosures and recommendations for secondary insiders.[272] This proposal, however, was rejected by the Federal government without further explanation. Nevertheless, secondary insiders who transmit inside information to third persons can be prosecuted under general joint offender[273] and accomplice[274] principles of German criminal law,[275] because the third person will then become a secondary insider as well and will be subject to the same transaction prohibition as the first secondary insider.

Concededly, a loophole exists for a secondary insider's recommendation to another person. The other person cannot be qualified as a secondary insider because he is unaware of the inside information. Consequently, the third party is free to exercise the tip, without any the threat of prosecution against him or the secondary insider advising him in the transaction. This situation can hardly be reconciled with the objective of the Securities Trading Act, namely to prevent insider trading and thereby strengthen the German financial markets. From the perspective of outside investors and their expectation of fair dealing, it is probably irrelevant whether a secondary insider concludes the transaction or causes another person to conclude the transaction. Either method will be regarded as unfair to outside investors and therefore, destroy their trust in the German financial markets. One can only hope that the German Federal government will become fully aware of this unacceptable situation and amend the Act before the regulatory leak causes more harm to the confidence of outside investors.[276]

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269. *Compare* Caspari, *supra* note 5, at 546, *and* ASSMANN & SCHNEIDER, *supra* note 5, § 14 para. 77.

270. Immenga, *supra* note 5, at 204; Jander & Zoberbier, *supra* note 5, at 808.

271. *Bundesrat* (federal council).

272. BT-DRUCKS, *supra* note 24, at 94.

273. *Mittäter* (joint offender).

274. *Teilnehmer* (accomplice).

275. §§ 25-27 StGB (*Strafgesetzbuch*) (Criminal Code).

276. *Accord* SIEBOLD, *supra* note 5, at 244; Assmann, *The New German Insider Law*, *supra* note 5, at 522. It furthermore has to be noted that most of the other European States decided

United States insider laws, as regulated through Rule 10b-5 and Rule 14e-3 of the SEA, the latter of which is applicable in a third-party tender offer context,[277] are in many respects similar to the coverage of the secondary insider prohibition in Germany. Generally, Rule 10b-5 extends the obligations of primary insiders to persons who do not stand in any fiduciary relationship to the issuer of the insider securities.[278] These persons are called "outsiders" in U.S. insider law terminology.[279] The coverage of outsiders is made possible through the application of the misappropriation theory.[280] Since the duties applicable to outsiders are nearly the same as those for insiders,[281] this article will refer to previous explanations of primary insiders.

One plain distinction between the German and U.S. secondary insider regulation should be mentioned here. While the statutory language of the German insider regulation leads to a direct, unquestionable prohibition for outsiders, its U.S. counterpart must employ the misappropriation theory with a necessary relationship of trust and confidence between the primary and secondary insider in order for the behavior to be punishable.[282] Therefore, under German insider regulation, someone who secretly listens to conversations that contain inside information and later makes securities trades based upon this knowledge would definitely violate the German insider trading prohibition, whereas this would not necessarily be true under U.S. insider law because of the lack of confidence and trust between the person who overheard the information and the insider.

In the United States, Rule 14e-3 of the SEA contains an acquisition and recommendation prohibition[283] for persons who would be defined as secondary insiders under German insider law. However, instead of using the secondary insider terminology, the Rule defines such people as those who are "in possession of material information relating to [a] tender offer [by another person] which information he knows or has reason to know is nonpublic."[284] Furthermore, the information has to be acquired directly or indirectly from (a) "a person who has taken a substantial step or steps to

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to implement equal insider trading prohibitions for both primary and secondary insiders.

277. 17 C.F.R. § 240.14e-3(a)(1-3).

278. *Id.; O'Hagan*, 92 F.3d at 616.

279. *O'Hagan*, 92 F.3d at 616. Under German insider law, such persons are generally called secondary insiders. Accordingly, "outsider" and "secondary insider" will be used interchangeably.

280. For a short discussion of the theory, *see supra* notes 178-79 and accompanying text.

281. "Insiders" in the terminology of the Act. This group would be called primary insiders in Germany.

282. *Clark*, 915 F.2d at 443; ten Oever, *supra* note 179, at 1326-28.

283. 17 C.F.R. § 240.14e-3(a).

284. *Id.*

commence or has commenced a tender offer,"[285] (b) the issuer of the securities being subject of the tender offer, or (c) any officer, director, employee, or other person acting on behalf of the offering person or the issuer.[286] These "secondary insiders," similar to those in the German provision, do not have to stand in any kind of a fiduciary duty to the offering person or the issuer.[287]

The restriction provided for secondary insiders is hereby more complete than the German provision, since Rule 14e-3 prohibits not only acquisitions made by such persons directly, but also recommendations and tipping that lead to the acquisition of the securities.[288] These secondary insiders can, however, avoid conflicts with the SEC if they publicly disclose the material information in a press release within a reasonable amount of time.[289] Thus, any transaction caused directly or indirectly by such persons is covered under Rule 14e-3, thereby avoiding the loopholes of its German counterpart.

c. *Sanctions of Violations*

Violations of the insider trading prohibition promulgated in Section 14 of the German Securities Trading Act are punishable under Section 38. Pursuant to this provision, they shall be adjudged with a fine or imprisonment of up to five years.[290] With this relatively high sentence, in comparison to other German business offense provisions, Germany has one of the highest penalties in the European Union.[291] Despite the fact that the insider trading restriction distinguishes between primary and secondary insiders, Section 38 does not contain different treatment provisions for the two groups. Consequently, once a secondary insider has committed a violation of Section 14, he is adjudged under the same standard and with the same high sentences as are available for primary insiders. This seems to be consistent with the intention of the Act, since insider dealing of both primary and secondary insiders must be treated as immoral acts, endangering the reputation and

285. Such a person is called an "offering person." 17 C.F.R. § 240.14e-3(a).
286. *Id.*
287. The avoidance of such a requirement in Rule 14e-3 is, however, challenged as an excess of the rulemaking authority of the SEC in *O'Hagan*, 92 F.3d at 612, which is pending now in front of the U.S. Supreme Court. The outcome of this case is of interest, since the omission of a fiduciary duty requirement was contested without merits in *SEC v. Peters*, 978 F.2d 1162 (10th Cir. 1992), in which the U.S Court of Appeals upheld the SEC Rule and thus reversed the district court's holding.
288. 17 C.F.R. § 240.14e-3.
289. *Id.*
290. WpHG § 38(1), v.26.7.1994 (BGBl. I S.1759).
291. For instance, the statutory definition of *Kapitalanlagebetrug* (fraud involving capital investments) only contains imprisonment for up to three years. § 264a StGB. *Compare* Assmann, *Part II*, *supra* note 5, at 250.

credibility of the German financial markets.[292]

As previously stated, an attempt to use insider information, a violation of Section 14, is not punishable, since Section 38 does not provide sanctions for such an act.[293] Pursuant to Section 38(2), any violation of a regulation under the law of a foreign country that corresponds to a German regulation listed in Section 38(1) shall be punishable in Germany. Therefore, any German citizen who commits insider trades in the United States that violate the U.S. SEA and the Rules promulgated thereunder can be punished by German courts with the same stringent penalties as provided for infringements of German insider law.[294]

IV. DISCLOSURE AND REPORTING DUTIES

In addition to its prohibitive measurements, the Securities Trading Act also regulates reporting and disclosure duties designed to quickly provide important information to the investment market, thereby reducing the risks of insider trade occurrences. These publication duties are contained in Section 15 (Ad-hoc Publicity) and Section 21 (Reporting of voting Rights Changes).

A. *Ad-Hoc Publicity*

Pursuant to Section 15(1) of the Act, issuers of securities that are admitted to official trading or to the regular market at a German exchange are obliged to report and disclose new, unknown circumstances that relate to the assets, financial condition, or business performance of the issuer and might materially affect the price of such securities. This disclosure is known as ad-hoc publicity. The definition of the term securities is the same as that for "insider securities" in the insider trading prohibition.[295] In contrast to the insider trading regulations, securities that are solely traded in over-the-counter transactions are not included.[296]

1. Information to Be Published

The ad-hoc publicity requirements establish only a duty to report and

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292. SIEBOLD, *supra* note 5, at 234.

293. The attempt of an insider violation also cannot be punished under general Criminal Law provisions dealing with the criminality of attempts of criminal offenses, §§ 22-23 StGB, since § 38 WpHG only qualifies as a *Vergehen* (misdemeanor) and hence cannot be pursuant under §§ 22-23 StGB. *See* SIEBOLD, *supra* note 5, at 269.

294. *See* ASSMANN & SCHNEIDER, *supra* note 5, § 38 para. 3; Immenga, *supra* note 5, at 204.

295. *See supra* part III.B.3.

296. WpHG § 15, v.26.7.1994 (BGBl. I S.1753).

disclose new circumstances that have occurred within the issuer's sphere of activity and that are not known to the public.[297] Furthermore, these circumstances must have the potential to materially affect the price of the issuer's securities through their effect on the assets and financial condition or the overall business performance of the issuer.[298] With regard to the provisions "circumstance," "not known to the public," and "possibility to materially affect the price," the discussion applies likewise to the insider information term.[299] Thus, facts that must objectively be able to alter the price of securities within a single Plus/Minus notification mark must remain unknown to the market participants.

These unknown facts have to relate both to the assets and to the financial condition or overall business performance of the issuer and must occur within the sphere of the issuer.[300] As can be seen from the formulation, this definition of facts to be published is narrower than the formulation for inside information in Section 13. The inside information provision only requires that the facts relate to insider securities or the issuers of such securities, whereas the ad-hoc publicity provision mandates the occurrence of the events within the issuer's sphere.[301] Therefore, all information that can be qualified as new circumstances within the meaning of Section 15 automatically assumes inside information status, however, not all insider facts are necessarily publishable by the issuer.[302] For example, despite the fact that market information constitutes inside information within the meaning of Section 13, it does not have to be reported under Section 15.

Facts that might affect the assets and the financial condition or overall business performance of an issuer and therefore have to be publicized include: merger or acquisition agreements, transfer of control and transfer of profits agreements, the acquisition or disposition of large blocks of shares, the conclusion of important contracts with customers or suppliers, inventions, product liability lawsuits filed against the issuer, and the issuance of nonvoting preferred shares or debt instruments.[303]

The Act generally mandates a duty to disclose without delay. An interesting question is exactly when is this duty triggered? This is especially pertinent regarding important decisions that must be approved by various groups. For instance, a merger plan might have been proposed by the

297. For a comprehensive discussion of WpHG §15, *see* DEUTSCHE BÖRSE AG, *supra* note 5, at 13; MOHR, *supra* note 4, at 28; Dryander, *supra* note 4, at 28; Hopt, *Basic Problems*, *supra* note 5, at 146; Peltzer, *supra* note 5, at 750.

298. WpHG § 15(1) sentence 1, v.26.7.1994 (BGBl. I S.1753).

299. *See supra* part III.B.3. with regard to these requirements.

300. WpHG § 15(1) sentence 1, v.26.7.1994 (BGBl. I S.1753-54).

301. DEUTSCHE BÖRSE AG, *supra* note 5, at 17.

302. MOHR, *supra* note 4, at 29.

303. Möller, *supra* note 5, at 109.

management body of a corporation, but still needs to be approved by the supervisory board and, in certain cases, eventually by the shareholders. In these cases, the legal obligation of Section 15 is assumed if the decision has reached a certain degree of likelihood.[304] Therefore, the duty to report does not generally arise until the supervisory board has given its assent to management's decisions, despite the fact that management plans are normally approved by the supervisory board in Germany.[305] Only in certain scenarios might a CEO's plan itself trigger the disclosure obligation, for example, if management's decision already has a large potential to alter the price. The conclusion of a friendly merger agreement between the CEOs of two companies could be such an example. However, the disclosure release of the issuer must then expressly indicate the necessity of final approval.[306] It has to be taken into account that although a management decision does not generally actuate reporting obligations, it might well already constitute inside information. Hence, trades based on such a decision are prohibited.[307]

Upon triggering the disclosure duties of Section 15(1) sentence 1, an issuer first has to inform the Federal Supervisory Authority and the board of directors of the stock exchange where the security or its derivative is traded, about the relevant circumstances, before publishing them to the public.[308] Section 15(3) determines the method of publication to the market participant. Accordingly, the issuer must disclose the facts in either one business newspaper with nationwide circulation or through an electronic information dissemination system that is widely used. After having published the information, the issuer must place a notice about the publication in the Federal Law Gazette[309] and send a copy to the Federal Supervisory Authority.[310] The issuer has the opportunity to apply to the Federal Supervisory Authority for an exemption from the reporting and disclosure duties of Section 15, if the obligation could be "likely to damage the legitimate interests of the issuer."[311] Of particular importance is Section 15(6). According to this section, third persons have no cause of action against issuers for damages caused by failure to comply with the ad-hoc publicity requirement.

304. Assmann, *Part II, supra* note 5, at 251.
305. MOHR, *supra* note 4, at 29.
306. DEUTSCHE BÖRSE AG, *supra* note 5, at 16.
307. *Id.* at 16-17.
308. WpHG § 15(2), v.26.7.1994 (BGBl. I S.1753-54); Immenga, *supra* note 5, at 205.
309. *Bundesanzeiger* (Federal Law Gazette).
310. WpHG § 15(3)-(4), v.26.7.1994 (BGBl. I S.1754) (detailing requirements).
311. *Id.* § 15(1) sentence 2, at S.1754; *see also* Möller, *supra* note 5, at 110.

2. The United States Equivalent

The U.S. counterpart of the German ad-hoc publicity is more or less the filing requirement of an 8-K report of current events by an issuer of securities that are registered pursuant to the SEA.[312] For example, issuers must file a Form 8-K within fifteen calendar days after large acquisitions or dispositions of their assets.[313] The SEA, however, also explicitly imposes reporting duties for events such as tender offers by issuers or third parties,[314] which under German law could only be requested indirectly under the ad-hoc publicity. Hence, the SEA contains in some respects a more detailed system of disclosure than the German Securities Trading Act.[315]

B. *Reporting Obligation: Changes in Holdings of Voting Rights*

The Securities Trading Act introduced a new duty to report changes in the holdings of voting rights of German corporations[316] listed in a German or European exchange.[317] A concerned person, the holder of voting rights that exceed or fall below the thresholds of 5%, 10%, 25%, 50%, or 75% due to acquisitions, disposals, or otherwise, must report it to the Federal Supervisory Authority and the affected corporation.[318] The report has to be filed no later than within seven calendar days and must contain the address of the voting rights holder as well as the actual percentage of voting rights.[319] The seven-day time period begins from the time the holder became aware of the knowledge, or from when the holder can be supposed to have become aware of the knowledge, of the exceeding or falling below the thresholds.[320] After being notified, and then by no later than nine calendar days, the exchange-listed company whose voting rights were affected is required to place a statement containing the facts received pursuant to Section 21 of the WpHG in at least one mandatory exchange newspaper of national circulation.[321] This provision, among others, was designed to protect target corporations and their shareholders from hostile takeovers, which presumably will occur in Germany more often in the near

312. 17 C.F.R. §§ 240.13a-11, 249.308 (Form 8-K).
313. *Id.* §§ 249.308, 240.13a-11.
314. *Id.* §§ 240.13e, 240.13e-100 (Schedule 13E-3 for tender offers of third parties).
315. For an example, see the quarterly filed 10-Q report, 15 U.S.C. § 78m, of the Securities Exchange Act.
316. WpHG § 21(2), v.26.7.1994 (BGBl. I S.1755).
317. *Id.* § 21, at S.1755.
318. *Id.* § 21(1) sentence 1, at S.1755.
319. *Id.*; *see also* MOHR, *supra* note 4, at 32.
320. WpHG § 21(1) sentence 2, v.26.7.1994 (BGBl. I S.1755).
321. *Id.* § 25, at S.1756-57 (stating information regarding the procedure and obligations).

future.[322]

For the purpose of determining the concerned person's percentage under Section 21, the Act provides an imputation of voting rights provision. For example, the voting rights of an enterprise controlled by the holder or the voting rights held by others on his behalf are deemed to be equivalent to the voting rights held by the concerned person directly.[323] Thus, this provision in the Act is similar to Section 13(d) of the U.S. SEA and the rules promulgated thereunder.[324] Section 13(d) of the SEA requires purchasers of securities that are registered under Section 12 to fulfill certain reporting obligations within ten days after the acquisition of the securities. For example, the purchaser is required to inform the issuer of the securities and to file a statement with the SEC.[325]

One major difference between the German and the U.S. provision is the event that triggers the reporting duties. The German Securities Trading Act requires only that the purchaser hold, after the transaction and without regard to the size of the transaction, a security amount that is below or above the 5%, 10%, 25%, 50%, or 75% thresholds. In contrast, in the United States the SEA mandates a filing obligation for acquisitions through which the purchaser will acquire more than 5% of securities of a corporation,[326] along with a duty to amend his filing statements after dispositions or purchases of more than 1%.[327] Thus, the German Act focuses on the triggering of certain thresholds, while the U.S. SEA focuses on the size of a transaction.

C. *Penalty Provisions*

Pursuant to Section 39 of the German Act, intentional or reckless violations of the reporting and disclosure provisions are punishable as misdemeanors with fines of up to DM 3,000,000 for non-compliance with the ad-hoc publicity requirement and of up to DM 500,000 for violations of Section 21 (Reporting of Voting Share Changes).[328]

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322. *See, e.g.*, DIE WELT, Apr. 11, 1997, at 10 (reporting the recent hostile takeover attempt of Thyssen by Krupp). Furthermore, major restructurings are expected in the banking area. In acknowledgement of this, Germany has recently promulgated a takeover code.

323. *See* WpHG § 22, v.26.7.1994 (BGBl. I S.1755-56); MOHR, *supra* note 4, at 33.

324. *See* 15 U.S.C. § 78m (1994).

325. *Id.* For the exact information that has to be mentioned in the statement, *see* Schedule 13D of the SEA. 17 C.F.R. § 240.13d-1(a). The purchaser must, for example, list the total number of securities directly or beneficially owned by him and provide facts relating to the intention pursued with the acquisition. *Id.* § 240.13(d)(1)(A)-(D).

326. 15 U.S.C. § 78m(d)(1).

327. 17 C.F.R. §§ 240.13(d), 240.13d-2.

328. Parts of § 15 of the German Securities Trading Act also are only punishable with a fine up to DM500,000. For more details, *see* the complete list in § 39. WpHG § 39, v.26.7.1994 (BGBl. I S.1759-60); DEUTSCHE BÖRSE AG, *supra* note 5, at 25.

V. CONCLUSION

The German Securities Trading Act, as part of the Second Financial Markets Promotion Act, has dramatically improved the reputation of the German financial markets. Overall, the insider law and the public disclosure and reporting duties of the Act are meaningful and mostly stringent, thereby achieving the German legislator's goal of keeping up with the regulatory schemes of other, world-class financial markets. Some provisions concerning the insider trading prohibition, however, reveal regulatory leaks. They can be explained by the lack of insider law experience of German legislators and by the reluctant attitudes of some parts of the Federal government because if was finally forced by European Law to give up the previously existing Insider Trading Guidelines and to enact insider rules.

One subject of criticism is the exclusion of a prohibition of primary insiders from dissuading third persons to make transactions and the nonadoption of restrictions for secondary insiders that are similar to those for primary insiders. The Federal government would be strongly advised to amend the Securities Trading Act with respect to these criticisms. Once investors and securities dealers become fully aware of the existing gaps in the Act, unethical and unpunishable practices can and will occur, thereby again weakening the reputation of the German financial markets.

Nevertheless, especially with regard to the situation prior to the enactment of the Second Financial Market Promotion Act, the German insider law can now be considered a real obstacle for most of the current insider trading practices. Thus, the Act is regarded as a successful attempt by the German legislature to improve the domestic financial markets. Evidence of this estimation lies in the violations of the insider trading prohibition and the reporting duties of corporations that already have been discovered. The investment industry, however, will need more legal certainty with regard to the definition of various terms under the Securities Trading Act, such as "suitability to materially affect the price." Unfortunately, scholarly articles can only provide limited assistance. Therefore, only the first cases that are decided by German courts about issues raised by the Securities Trading Act will provide reliable guidance.