
Chien-Chung Lin

Chien-Chung Lin, Eric Hung

National Chiao-Tung University, Taiwan, 2014/4/10

Contents

1. Introduction ................................................................................................................................................................................. 3
2. SEC and the Enforcement of Insider Trading Law ...................................................................................................................... 3
   2.1 The Power of Securities and Exchange Commission and Other Agencies ................................................................. 4
      2.1.1 Organization and Responsibilities of the SEC ............................................................................................................. 4
      2.1.2 Self-Regulatory Organizations ................................................................................................................................. 6
   2.2 Enforcement Actions and Proceedings ............................................................................................................................... 7
      2.2.1 Administrative Proceedings and Types of Sanctions ................................................................................................. 7
      2.2.2 Federal Judicial Proceeding and Remedies ............................................................................................................. 8
      2.2.3 Parallel Criminal Proceedings .................................................................................................................................. 9
   2.3 SEC’s Investigative Process ................................................................................................................................................ 9
      2.3.1 General Guidelines .................................................................................................................................................. 9
      2.3.2 Initiation and Informal Investigation ...................................................................................................................... 10
      2.3.3 Formal Investigation ............................................................................................................................................... 11
      2.3.4 The Wells Process ................................................................................................................................................ 12
      2.3.5 Recommendation and Deciding an Enforcement Action ...................................................................................... 13
   2.4 Insider Trading Investigation Methods ............................................................................................................................ 14
3. Insider Trading Enforcement Trend from 2009 to 2012 .......................................................................................................... 16
   3.1 General Overview and Research Method .......................................................................................................................... 16
      3.1.1 Research Method .................................................................................................................................................. 16
      3.1.2 General Overview ................................................................................................................................................ 16
      3.1.3 Defendant’s Background and Types of Info ......................................................................................................... 17
      3.1.4 Case Results, Illicit Gain and Settlements ........................................................................................................ 19
      3.1.5 Penalties ............................................................................................................................................................. 20
3.1.6 Parallel Criminal Charges

3.1.7 Time Duration

3.1.8 Additional Database Results

3.2 Role of Settlement in SEC’s Insider Trading Cases

3.2.1 Why Settling a Case?

3.2.2 Factors of Consideration from SEC Side

3.2.3 Criticism

3.2.4 Reflection

3.3 Parallel Criminal Investigation and Optimality of Punishments

3.3.1 The Optimal Punishment in Securities Law

3.3.2 Parallel Proceedings and Its Problems

4 Conclusion
1. Introduction

Securities law, for most of its part, is designed to combat securities fraud. However, the idea about what is the proper method in achieving this goal is sometimes, if not often, divided. Generally, the U.S. approaches this issue with a two-layered structure which allows private litigation and government intervention at the same time. Government intervention is achieved by multiple regulatory agencies which include, most importantly, Securities and Exchange Commission (SEC), Department of Justice, Self-Regulatory Organizations such as stock exchanges and Financial Industry Regulatory Authority. Under the glamorous universe of ways of enforcing securities law, Securities and Exchange Commission possesses the central position and leads the direction of both policy-making and actual enforcement, including carrying out investigation and shaping the outcome of violations of securities law.

For many years, the structural complexity of multiple-agency enforcement in the United States has been a key feature in the field of securities law. Similarly, the effectiveness of this multiple-agency enforcement is also at the center of scholarly as well as policy debate. Especially the collaboration among agencies and the choice of enforcement tools, instead of others, are both attracting research interest. To evaluate the use of certain enforcement tools and their optimality, this Article surveys the recent enforcement of insider trading cases by the SEC from 2009 to 2012 to understand the real picture of securities law enforcement. With the particular focus on the use of settlement, we examine the use of settlement in insider trading cases in the SEC’s actions and how it works as a tool of effectively meeting the goals of litigation efficiency and adequate deterrence. During the course of this analysis, the goal of punishing insider trading activities, as well as its limits, are also reviewed.

This Article proceeds as follows. Part I is introduction. Part II briefly discusses the current securities law enforcement system in the United States and how SEC is designed to prevent violations of securities law, including procedures and tools. Part III provides empirical data from SEC enforcement news release from 2009 to 2012 to give a more complete picture about SEC’s enforcement in insider trading law. By observing these data, we also discuss the merit and limits in current approach. Part IV concludes.

2. SEC and the Enforcement of Insider Trading Law

Based on the framework established by Securities Act of 1933 and Securities Exchange Act of 1934, the power and responsibility of monitoring the securities market and enforcing securities laws are placed in the hand of the Securities and Exchange Commission.1 Basically, the SEC, especially the Division of Enforcement under it, brings civil enforcement actions when violations of securities laws are spotted. At the same time, the Securities and Exchange Commission cooperated with other agencies or entities, including Department of Justice (DOJ) and other self-regulatory organizations (SROs, mostly Financial Industry Regulatory Authority/FINRA and national securities exchanges), to enforce securities laws and ensure a proper function of the securities market in different proceedings.2

---


2 Id. at 40.
Generally, the SEC only exercises civil authority and has the authority to refer cases and evidence to the DOJ when criminal sanctions are pondered.3

2.1 The Power of Securities and Exchange Commission and Other Agencies

The United States Securities and Exchange Commission (the “SEC” or “Commission”) was established by the Securities Exchange Act of 1934, it is the federal government’s principal investigative and enforcement arm with respect to the securities industry. The Commission is in charge of the overall integrity of the securities market, it also plays an oversight role in regulating members in the capital market. Therefore, the SEC will be required to balance competing interests among various players. The SEC’s stated mission reflects this tension. Today, the mission of the SEC is composed of three objectives: “to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.”4

2.1.1 Organization and Responsibilities of the SEC

The SEC has five Commissioners with staggered five-year terms at its top of the management. One of them is the Chairman of the Commission who is appointed by the United States President. Additionally, no more than three of the Commissioners may belong to the same political party. Today, with the headquarters in Washington, D.C., the SEC has five Divisions, 23 offices, 11 regional offices and approximately 3,500 staff throughout the country.5

As the primary administrative agency for the securities regulation, the SEC has several responsibilities which can be categorized into four main areas: rule-making, securities law enforcement, market supervising, and coordinating with other authorities.6 These responsibilities are carried out by five divisions within the Commission, which includes Division of Corporation Finance, Division of Trading and Markets, Division of Investment Management, Division of Enforcement and Division of Economic and Risk Analysis. These divisions, despite each having different tasks, all work toward the same ultimate goal—maintaining the integrity of the capital market.

The Division of Corporation Finance handles corporate disclosures from regulated companies that are readily available to the investing public. This Division reviews the documents that public-held companies filed with the Commission, which includes registration of newly-offered securities, periodic filings (Forms 10-K and 10-Q), proxy materials, annual reports, and filings related to mergers and acquisitions or tender offers.7 One of the more commonly used techniques for Division of Corporate Finance to communicate with members of the securities industry is the issuance of “no-action letter.” A no-action letter is typically requested by individuals or companies who are not sure

3 Id. See also 15 U.S.C. § 78u(d)(1).
6 See id.
7 See id. See also CHOI & PRITCHARD, supra note 1, at 40.
about whether their new business decisions, transactions or plans would violate SEC rules. By granting a no-action letter to the requesting party, the SEC staff suggests that no further enforcement actions would be recommended to the Commission based on the facts detailed in the original applying letter.\(^8\)

The Division of Trading and Markets primarily acts in an oversight role on major securities market participants such as the securities exchanges, securities firms, self-regulatory organizations (SROs), etc. Besides its oversight role, this Division also reviews and sometimes approves rules filed by the SROs, as well as helps the Commission in establishing rules and standards of the securities market.\(^9\)

The Division of Investment Management, as implied by its name, deals primarily with investment-related issues. The main goal of this Division is to make sure the investors, especially the retailed customers, are getting useful information from professional fund managers, analysts or investment advisers. This Division also responds to no-action requests and facilitates with enforcement staff to advance the Commission’s interests.\(^10\)

The Division of Enforcement handles various kinds of enforcement activities coming from different parts of the securities industry. The Enforcement Division executes civil power in bringing civil actions in the federal courts or administrative proceedings within the Commission to ensure securities laws and rules are followed. With the help of the Enforcement Division, the SEC is able to make sure individuals or entities that violate securities law are subjected to appropriate sanctions, which in turn creates a deterrence effect to potential violators. The SEC’s enforcement staff receives referrals from many sources such as investor complaints, Divisions and Offices of the SEC, the SROs and other securities industry sources. Once the staff receives the evidence, they need to decide whether or not to investigate further and commence an enforcement action. In addition to civil and administrative actions, the SEC can make referrals to the Justice Department for the execution of criminal cases.

The Division of Economic and Risk Analysis was created in 2009, and it serves to integrate economic and data analysis into the work of the SEC. Due to the limited resources that the SEC possesses, finding the best allocation of the Commission’s resources is important. This Division provides economic analyses and risk assessment to support SEC’s rule-making, enforcement, litigations and examinations in order to achieve that goal.\(^11\)

Other than the five Divisions mentioned above, there are still many offices and branches within the Commission which serve to carry out the SEC’s mission of providing the investing public with fair, orderly, and efficient markets. In addition, the SEC has been actively communicating with the participants in the capital markets and has asserted its cases in the courts. By doing so, information reflecting the Commission’s view is directly transmitted, and the SEC maintains its primacy in promoting and enforcing securities law.

---

\(^8\) Id. at 41.

\(^9\) See The Investor’s Advocate, supra note 5.

\(^10\) See id.

\(^11\) See id.
2.1.2 Self-Regulatory Organizations

Although the SEC is the primary regulator of the securities market, it is not the only one. §19 of the Securities Exchange Act of 1934 provides the foundation for the establishment of other regulatory agencies such as the national securities exchange, registered securities association, and registered clearing agency. These agencies are still subject to oversight by the SEC. Today, there is FINRA (Financial Industry Regulatory Authority), PCAOB (Public Company Accounting Oversight Board) and the national securities exchanges, such as NYSE (New York Stock Exchange) and NASDAQ (National Association of Securities Dealers Automated Quotations), acting as other regulators of the securities industry.

FINRA is an independent, not-for-profit organization authorized by Congress to protect the investors in the securities industry. The principal regulation target for FINRA is brokers and dealers. Nearly all broker-dealers in the United States are members of FINRA. In order to fulfill its mission to protect investors and market integrity, there are five activities that FINRA performs on an everyday basis: (1) Deter misconduct by enforcing the rules, (2) discipline those who break the rules, (3) detect and prevent wrongdoing in the U.S. markets, (4) educate and inform investors, and (5) resolve securities disputes. In the year of 2012, FINRA brought 1,541 disciplinary actions against firms and individuals that violated FINRA rules, and imposed more than $68 million in fines and $34 million in restitution to harmed investors. Moreover, FINRA also referred 692 fraud and insider trading cases to the SEC and other agencies for further actions.

Besides FINRA, NYSE and NASDAQ also established requirements for those listed companies to follow. In general, those requirements are set to make sure listed companies are in healthy financial conditions and desirable corporate governance structure. The use of independent directors is one of the stressing points among these requirements. NYSE and NASDAQ require listed companies to have a majority of independent directors and also establish audit, compensation, and director nominating committees.

Finally, the PCAOB which was created by Congress as part of the Sarbanes-Oxley Act of 2002, is responsible for overseeing the audit of public companies and broker-dealers. Public accounting firms are also required to register with the PCAOB. To make a long story short, the PCAOB protects the investing public by making sure the registered companies have informative, accurate and independent audit reports.

Both the SEC and SROs have the principal mission of promoting the integrity of the capital market and providing investors with better investing environment. However, as the capital market has grown more and more sophisticated, the mission of investor protection has become more complicated and multi-dimensional. To deal with this situation,

---

13 CHOI & PRITCHARD, supra note 1, at 42.
14 What We Do, FINRA, http://www.finra.org/AboutFINRA/WhatWeDo/
16 CHOI & PRITCHARD, supra note 1, at 43. See also About the PCAOB, PCAOB, http://pcaobus.org/about/pages/default.aspx.
Congress revised the SEC’s statutory mandate to expressly require the SEC “to consider or determine whether an action is necessary or appropriate in the public interest and to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.” This multi-dimensional approach not only applies to rule making, but also is reflected in enforcement matters, which apparently involves some degrees of balancing competing interests. In this regard, it becomes inevitable for the Commission’s enforcement staff to weigh in factors when carrying out actions through various enforcement tools.

2.2 Enforcement Actions and Proceedings

2.2.1 Administrative Proceedings and Types of Sanctions

The SEC exercises its civil authority in enforcing securities law both in its own administrative proceedings and in actions brought in federal court. Administrative proceedings are prosecuted by the SEC and adjudicated by a SEC administrative law judge or hearing officer. Through the passage of time, the SEC currently possesses multiple sanction weapons to combat against insider trading in administrative proceedings, which is less time-consuming and more convenient compared to normal civil proceeding via federal district court system. Those weapons include (1) cease-and-desist order, (2) temporary order, (3) disgorgement order, (4) officer and director bar order, bar from association with securities industry, and professional discipline.

In cease-and-desist proceeding, the SEC generally seeks a cease-and-desist order. In a cease-and-desist order, after notice and opportunity for hearing person and if approved by a SEC administrative law judge, the SEC can require violator and any other person that is, was, or would be a cause of the violation to cease and desist from committing or causing such violation and any future violation of the same provision, rule, or regulation. Also, prior to the completion of the cease-and-desist proceeding, the SEC can seek temporary order to prohibit violator to dissipate or convert his assets to prevent the harm to investors or the public. In addition, the SEC can seek disgorgement and an officer and director bar order in cease-and-desist proceedings.

---

19 Choi & Pritchard, supra note 1, at 186.
20 Thomas Lee Hazen, Treatise on the Law of Securities Regulation, § 16.2[13].
21 SEC has power to suspend, limit, or bar “any person” from practicing before it “in any way.” 17 C.F.R. § 201.102(e)(3). Rule 102(e) has been used by the SEC to discipline professionals, mostly against accountants and lawyers. More detail in SEC’s power in disciplining professionals, see Hazen, supra note 20, § 16.2[18].
24 15 U.S.C. § 78u–3(e). Though both are monetary assessment to defendants, generally, disgorgement goes to the plaintiff and civil penalties go to the Treasury. 15 U.S.C. § 78u–1(d)(1). Noticeably, according to the “fair fund” provision of Section 308 of the Sarbanes-Oxley Act, the SEC can designate a penalty or settlement it receives to be added to and become a part of a disgorgement fund for the benefit of investors harmed by the defendant’s violation. 15 U.S.C. § 7246. For more information
Further, in administrative proceeding, the SEC can impose three-tier monetary penalty. Monetary penalties of $100,000 for a natural person or $500,000 for any other person can be imposed when involving fraud such as insider trading. The maximum goes up to $100,000 for a natural person or $500,000 for any other person if substantial losses or a significant risk of substantial losses to other persons or substantial pecuniary gain is incurred by such a violation.

All orders from the SEC’s administrative proceedings are subject to judicial review from a court of appeal. However, as noted by scholarship, reviews generally do not include factual findings and circuit courts tend to defer to the SEC’s interpretation of law. In this regard, a successful challenge to the SEC’s administrative decision in review process may not be easy as generally thought.

2.2.2 Federal Judicial Proceeding and Remedies

When dealing with more severe violation of securities laws, the SEC is likely to seek relief in federal district court. With judicial proceeding, according to SEA§ 21 and 21A respectively, the SEC can either seek an injunction or monetary penalty in federal court.

In injunctive proceeding, the SEC has a broader range of sanctions available than it does in administrative cease-and-desist proceedings. Those include injunctions against future violations, officer/director bar (sometimes termed “corporate governance reforms”), and other equitable relief (most importantly disgorgement orders).

For monetary penalties (also termed as “civil penalty” in statute), in insider trading cases, the SEC needs to file suit in federal court to assess penalties which can amount to a maximum of three times the illicit profits realized or losses avoided. This monetary penalty can also be imposed on controlling persons who directly or indirectly controlled the

---

29 CHOI & PRITCHARD, supra note 1, at 208.
30 CHOI & PRITCHARD, supra note 1, at 216-17.
33 15 U.S.C. § 78u(d)(5). See also SEC v. First Pac. Bancorp, 142 F.3d 1186, 1191 (9th Cir. 1998)(“The district court has broad equity powers to order the disgorgement of “ill-gotten gains” obtained through the violation of the securities laws”).
34 15 U.S.C. § 78u–1(a)(2)(“The amount of the penalty which may be imposed on the person who committed such violation shall be determined by the court in light of the facts and circumstances, but shall not exceed three times the profit gained or loss avoided as a result of such unlawful purchase, sale, or communication.”)
person who committed violations of securities law, rules and regulations.\textsuperscript{35} Also, the civil penalties can be waived by the SEC\textsuperscript{36} or assessed in addition to other sanctions.\textsuperscript{37}

\subsection*{2.2.3 Parallel Criminal Proceedings}

Insider trading also triggers serious criminal liability.\textsuperscript{38} As a general matter by the operation of authority division provided by law, the SEC’s formal investigation can parallel the Justice Department’s investigation, as the former exercises authority in civil proceedings to pose sanctions and the latter criminal. However, parallel investigations also lead to problems, mostly wasting scarce investigation resources and the problems of contradiction among agencies. To avoid these problems, the Justice Department often coordinates its investigation with the SEC since the SEC has more direct control over the various sources to learn and analyze securities market irregularities and potential violations of securities laws.\textsuperscript{39} However, there are no legal requirements of sequence or deference as both the SEC and federal prosecutor can legally possess its own investigation authority concurrently.\textsuperscript{40}

\section*{2.3 SEC’s Investigative Process}

\subsection*{2.3.1 General Guidelines}

SEC investigations and enforcement proceedings are conducted by the Division of Enforcement, which is the main force in executing the SEC’s enforcement power. Typically, there are three steps that the enforcement staff will do in an enforcement proceeding. First, based on the facts gathered from the public or other sources, the staff will recommend the commencement of investigations of securities law violations. After a series of investigations, the staff will then decide whether or not to recommend the Commission to bring suits, and whether it will come into a federal court or before an administrative law judge. Lastly, the Division will prosecute these cases on behalf of the Commission and recover losses for the investors or impose penalties on the violators.\textsuperscript{41}

\begin{flushleft}
\textsuperscript{35} 15 U.S.C. § 78u–1(a) (1)(B), (3).
\textsuperscript{36} 15 U.S.C. § 78u–1(c).
\textsuperscript{38} 15 U.S.C. § 78ff(a)(”Any person who willfully violates any provision of this chapter (other than section 78dd–1 of this title), or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the terms of this chapter, …, shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both, except that when such person is a person other than a natural person, a fine not exceeding $25,000,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.”)
\textsuperscript{39} CHOI & PRITCHARD, supra note 1, at 200.
\textsuperscript{40} 15 U.S.C. § 78u(d)(1)(the SEC may “transmit such evidence as may be available concerning such acts or practices as may constitute a violation of any provision of this chapter or the rules or regulations thereunder to the Attorney General, who may, in his discretion, institute the necessary criminal proceedings under this chapter.”)
\end{flushleft}
How does the Division of Enforcement choose which cases to devote its investigative efforts on? Due to limited resources, it is practically impossible for the Division to pursue every matter it encounters. To allocate the resources to more significant cases, the Director of the Division or relative staff will rank the existing investigations and designate some particular cases as “National Priority Matters”. According to the SEC Enforcement Manual, when determining whether an investigation is a “National Priority Matter”, the Director and the staff take several factors into consideration. For example, whether the case presents an opportunity to send a strong message of deterrence with respect to the markets, products and transactions; the magnitude of the misconduct; whether the case involves egregious misconduct that will pose extensive harm to the investors. Moreover, the staff will consider the role of the violators, e.g., if the violators occupy positions of substantial authority or responsibility, or owe fiduciary duties to investors or others.42

Among these criteria, one should pay extra attention to the first one.43 While above criteria can serve as important factors for the Director or his designee when making their judgment on whether a particular event is designated as “National Priority Matter”, other facts and circumstances known to date are also in play. In other words, the SEC might focus their enforcement actions on particular types of violations in response to the investors’ expectations or for the sake of the entire securities market, which reflects the fact that the SEC, as an agency charged with the power and responsibility to regulate the securities market, is responsive to public perception as well as political atmosphere.

2.3.2 Initiation and Informal Investigation

Generally, the SEC’s investigations begin with informal or preliminary inquiry by the staff of the Division of Enforcement and those informal investigations are mostly confidential without notifying the targets of investigation.44 To initiate an investigation, the first thing to do is to gather information which might help identify possible violations of securities law. The sources of information are multiple. The staff can gather information by reviewing companies’ periodic filings and the market surveillance reports which are done by the SEC or the SROs. It can come from investors’ complaints or tips from whistleblowers. Moreover, it can come from reading newspaper and other media reports to see if there is any violation of securities law. Additionally, one of the major sources is the referral from other regulatory agencies such as PCAOB, FINRA, Stock Exchanges and sometimes Congress.45

43 As SEC Chairman Mary Jo White stated in her testimony in 2013, Enforcement Division of the SEC has continued to file enforcement actions that sent a strong message in an increasingly complex and global securities market. Moreover, recent SEC enforcement actions reflect an aggressive and continued pursuit of institutions and individuals whose actions contributed to the financial crisis, a focus on exchanges and market structure issues and continued efforts to combat insider trading by those who abuse positions of trust and confidence for personal gain. Mary Jo White, Testimony on Oversight of the SEC, http://www.sec.gov/News/Testimony/Detail/Testimony/1365171516050#.UhYDgZIpmny4 (May 16. 2013).
44 Id. But if companies are contacted for further information by investigation staff, companies frequently disclose this pending investigation in press releases or in corporate filings. This allows the targets of investigations and the general public to become aware of the investigation.
45 SEC ENFORCEMENT MANUAL § 2.2.2.
After receiving the information about violations, the enforcement staff will need to determine if the underlying facts are sufficient enough to constitute “Matter Under Inquiry”. A “Matter Under Inquiry” simply serves as a preliminary gate-keeping function to ensure that the Commission’s resources are designated to cases worth pursuing. Therefore, the staff needs to consider whether the facts could lead to an enforcement action which will address a violation of securities laws. This stage is also known as an informal investigation or preliminary investigation stage.

The staff will conduct informal interviews and request documents from people they deemed relevant to the case. All the investigations done in this stage are private, the information is kept confidential by the staff. For the most part, enforcement staff relies heavily on the target’s cooperation during this stage since there is no legal authority such as issuing subpoenas in forcing investigation targets to answer the inquiry.

Once the staff has concluded the informal investigation, it has several options to take, such as authorizing an administrative proceeding, seeking injunctive relief in court, referring the case to the Department of Justice for the institution of criminal proceeding, closing the investigation without further actions, or seeking a formal order of investigation from the Commission.

2.3.3 Formal Investigation

As an investigation develops, if the case is strong enough to pass the stage of informal investigation without a settlement, the enforcement staff will seek the approval to initiate a formal investigation. Currently a formal order of investigation can be obtained based upon the issuance by the Division’s senior officers.

Formal investigations generally are non-public. According to section 21(a) and (b), staff has the power to issue subpoenas to request documents and testimony under oath in a formal investigation. Noticeably, although the SEC has the power to issue subpoenas in a formal investigation, the SEC has to go to district court to get an order for mandatory compliance if the recipient of a subpoena refuses to comply to a subpoena voluntarily. The staff only needs to prove probable cause to the federal court that the securities laws have been violated in order to enforce the

46 SEC ENFORCEMENT MANUAL § 2.3.1.


50 17 C.F.R. § 203.5

51 SEC ENFORCEMENT MANUAL § 2.3.4.
subpoena against targets who are reluctant to cooperate.\textsuperscript{52} While issuing subpoenas is a useful way for the enforcement staff to pave its way toward a successful enforcement action, it does come with costs. Since the SEC often issues subpoenas to targets’ business partners, customers, auditors or other relevant parties for testimony, it will somehow harm the reputation or relationships between them.\textsuperscript{53} So even though formal investigation processes are mostly nonpublic, it may still have some collateral effects among parties involved.

2.3.4 The Wells Process
Toward the final stage of a formal investigation, if the enforcement staff has gathered sufficient information of the case, the enforcement staff will, under its discretion, issue “Wells Notice” to inform targets of the investigation and possible enforcement action against them. The content of the so called “Wells Notice” will include the evidences that the staff found, the legal theories behind the violations, the charges the staff is considering to recommend to the Commission, etc. However, in some situations, often when there are concerns about dissipation of assets or destruction of documents by the target, the staff will choose not to give the notice.\textsuperscript{54}

After receiving the notice, the targets of the investigation will then be allowed to submit “Wells Submission” to present his/her side of story and persuade the SEC an enforcement action is not appropriate.\textsuperscript{55} The content of the submission often will contain factual and legal arguments explaining why an enforcement action is not appropriate for the case presented.\textsuperscript{56} In the submission, target’s counsel needs to be aware of the effects that go along with the submission. The contents provided in the submission will often be taken as an admission or impeachment purpose against the target in later actions. Moreover, the submission may serve as a “roadmap” for the Commission in the litigation stage. Sometimes the federal prosecutor will refer to the Wells Submission in a parallel criminal proceeding as well.\textsuperscript{57} Therefore, counsels must consider carefully what information should be included in that submission.\textsuperscript{58} Nevertheless, a Wells Submission still has positive effects for the target. It provides the target opportunities to meet with the staff which then allows the target to give further explanations to conducts alleged. This sometimes will change staff’s recommendation to the Commission. Furthermore, counsel or the target may sometimes persuade the staff to exclude some defendants or reduce the severity of the charges.\textsuperscript{59}

\textsuperscript{52} See SEC v. Brigadoon Scotch Distributing Co., 480 F.2d 1047 (2d Cir. 1973).


\textsuperscript{54} McLucas, \textit{supra} note 48, at 112.

\textsuperscript{55} http://www.law.cornell.edu/wex/wells_submission

\textsuperscript{56} Sturc et al., \textit{supra} note 53.

\textsuperscript{57} Sturc et al., \textit{supra} note 53, at 15-12.

\textsuperscript{58} McLucas, \textit{supra} note 48, at 113.

\textsuperscript{59} Id.
After weighing the totality of evidence and nature of the event, the SEC will then come to decide whether and what sanctions in which proceeding is appropriate.

2.3.5 Recommendation and Deciding an Enforcement Action

Most of the actions taken by the staff need authorization from the Commission, which includes instituting enforcement actions, settling with defendants, and other aspects regarding civil litigation. The way of obtaining the authorization is to submit an action memorandum which addresses the factual and legal basis of the recommendation to the Commission. Normally, the Director or Deputy Director is responsible for authorizing the action memoranda. However, the Associate Director or Regional Director, in some instances, may decide on less significant issues.

When the staff makes a recommendation of instituting an enforcement action, there are three ways for the Commission to grant approval: by closed meetings, by seriatim consideration, or by Duty Officer’s consideration. Firstly, a closed meeting is held within the Commission where three or more Commissioners form a quorum and approve the staff’s recommendation with a majority vote. The meeting is not open to the public, which is based on the exemptions in the ‘Government in the Sunshine Act’. The enforcement staff will present the case it recommends to the Commission, and also prepare to answer the questions from the Commissioners. Second, Seriatim consideration is often used when there is a timely need for an enforcement action or when the case does not qualify for the exemptions under the Sunshine Act, and therefore cannot be considered in a closed meeting. The recommendation will be circulated within the Commission for rapid seriatim consideration. However, even if the recommendation received a majority vote from the Commission, it is not authorized until each Commissioner records a vote or abstains from voting. Lastly, the Commission can assign one of its members as the Duty Officer who has the authority to approve recommendations at his or her discretion. Nevertheless, a Duty Officer consideration is not appropriate when the case involves disputed legal issues or when the staff is trying to obtain an approval for settlement. It is often used when the staff is seeking an emergency action or temporary restraining order.

60 SEC ENFORCEMENT MANUAL § 2.5.1.
61 Id.
62 SEC ENFORCEMENT MANUAL § 2.5.2.
64 SEC ENFORCEMENT MANUAL § 2.5.2.1.
65 SEC ENFORCEMENT MANUAL § 2.5.2.2.
66 SEC ENFORCEMENT MANUAL § 2.5.2.3.
2.4 Insider Trading Investigation Methods

Insider trading is no doubt a focal point of the SEC’s enforcement program. General definition of insider trading refers to the buying and selling of securities while in possession of material, non-public information or tipping such information to others. Moreover, it usually involves a breach of fiduciary duty and the relationship of trust and
As a matter of fact, insider trading enforcement actions initiated by the Commission often involves the wrongdoing of companies’ top executives or directors who are referred to as traditional “insiders”. Furthermore, professionals who constantly gain access to confidential information such as accountants, consultants, investment bankers and lawyers are also under the radar of the Commission’s enforcement effort. These people are viewed as “outsiders.” In addition to the features of the defendants, insider trading cases tend to involve a huge amount of illicit profits being misappropriated and a broad base of harmed investors. All these unique characteristics add up to the urgency for the Commission to fight against insider trading.

Since insider trading has continued to be the priority of the SEC’s enforcement actions, it is essential to understand how the enforcement staff treats the investigation of insider trading cases. As similar to other types of cases, the information comes from many sources. Most important ones are informants such as market professionals, disgruntled employees, anonymous calls, and sometimes the competitors. Market surveillance done by the SROs also plays a large part in the investigation. SROs refer many suspicious trades to the Commission each year, and provide detailed reports to the Commission to facilitate the investigations. The SEC itself has also devoted significant personnel into monitoring the market trading, which aims at catching unusual trades made by the investors.

According to the insider trading investigation outline set out by the senior attorney of the Division of Enforcement, the objectives of the insider trading investigation are to establish “materiality”, “possession”, “scienter”, and “duty” of the alleged misconduct. Moreover, identifying suspicious trades, insiders and traders are also important, it allows the Commission to determine the scope of the misconduct. Lastly, setting the stage for disgorgement to recover illicit profits from the defendants is also an important objective of the investigation. Among various investigative techniques, there are several approaches worth noting. First, identifying suspicious trades is considered a challenging process. Although large trades are often seen as suspicious, small trades still cannot be ignored since they might link to other suspicious trades. Second, making phone interviews with traders to seek denials and admissions from them is often fruitful, because any false statement obtained from the traders’ denial will later on become evidence for the perjury charges. Third, there are many channels for the enforcement staff to obtain related documents such as requesting phone records, analyst reports, confidentiality agreements…etc. It is advised that the staff should act appropriately in requesting these documents in order to build a better case.


68 CHOI & PRITCHARD, supra note 1, at 352.


70 Id.

71 Id. at 4-5.

72 For more detail, see id. at 7-14.
In sum, building an insider trading case is a long process which requires significant efforts from the enforcement staff. The Commission has come up with a series of guidelines and manuals helping the staff to utilize the mechanics of investigation, as well as providing the targets/defendants with the rights they could exercise. However, along with the turmoil and massive loss brought by the Financial Crisis of 2008, the SEC has suffered much criticism and pressure to reform its practice to prevent financial meltdown from taking place again. In this regard, the change in the SEC’s enforcement has come into the spotlight again since. But interestingly, the empirical data in the next Part does show a more ambiguous picture than previously thought.

3. Insider Trading Enforcement Trend from 2009 to 2012

3.1 Research Result

3.1.1 Research Method

This research is aimed at insider trading enforcement actions the SEC brought from 2009 until 2012. The data being collected is primarily based on the content of cases that appeared in annual Select SEC and Market Data Report and the corresponding litigation releases in the SEC’s database. Besides the SEC’s database, we also use LexisNexis, Westlaw and JUSTIA Dockets & Filings to search case details when needed. By tracking every insider trading enforcement action and their litigation result, this research attempts to describe the SEC’s actual approach and attitude in enforcing inside trading cases. By this means, a more complete picture, as well as a useful comparison, can be learned.

3.1.2 Overview

In the years from 2009 to 2012, the SEC had brought a steady while increasing number of insider trading enforcement actions. It went from 37 cases in 2009, 53 cases in 2010, 57 cases in 2011, to 58 cases in 2012. Total defendants in 2009 were 85, and the number increased to 138 in 2010, then slightly decreased to 126 in 2011 and increased again to 131 in 2012. See the numbers shown in figure 1.

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Civil Action</td>
<td>31</td>
<td>34</td>
<td>48</td>
<td>52</td>
</tr>
<tr>
<td>Administrative Proceeding</td>
<td>6</td>
<td>19</td>
<td>9</td>
<td>6</td>
</tr>
</tbody>
</table>


74 Not all cases provide every piece of information that we need, as the nature of the aforementioned databases shows. For example, courts often set a different (and later) date for determining disgorgement amount and civil penalties than judgment date. Therefore, settlement amount and civil penalties sometimes are not available in every case from the statistics.

<table>
<thead>
<tr>
<th>Total Cases</th>
<th>37</th>
<th>53</th>
<th>57</th>
<th>58</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Defendants</td>
<td>85</td>
<td>138</td>
<td>126</td>
<td>131</td>
</tr>
</tbody>
</table>

Table 1: Insider Trading Enforcement Actions Initiated by the SEC – 2009 to 2012.


The numbers above become clearer in light of all actions the SEC brought in enforcing securities law. Insider trading cases are consistently of 6 to 8 percent of all cases. Compared to its high publicity, insider trading enforcement actually plays a less significant role in the sense of number of total cases enforced.

<table>
<thead>
<tr>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Civ</td>
<td>Admin</td>
<td>%</td>
<td>Civ</td>
</tr>
<tr>
<td>Securities Offering</td>
<td>106</td>
<td>35</td>
<td>21%</td>
</tr>
<tr>
<td>Issuer Reporting &amp; Disclosure</td>
<td>68</td>
<td>75</td>
<td>22%</td>
</tr>
<tr>
<td>Investment Advisors/ Companies</td>
<td>29</td>
<td>47</td>
<td>11%</td>
</tr>
<tr>
<td>Delinquent Filings</td>
<td>0</td>
<td>92</td>
<td>14%</td>
</tr>
<tr>
<td>Broker Dealer</td>
<td>26</td>
<td>83</td>
<td>16%</td>
</tr>
<tr>
<td>Insider Trading</td>
<td>31</td>
<td>6</td>
<td>6%</td>
</tr>
<tr>
<td>Market Manipulation</td>
<td>34</td>
<td>5</td>
<td>6%</td>
</tr>
<tr>
<td>Other</td>
<td>18</td>
<td>9</td>
<td>4.1%</td>
</tr>
</tbody>
</table>

Table 2: Classification and Numbers of All SEC Enforcement Actions—2009 to 2012.


3.1.3 Defendant's Background and Types of Info

Insider trading, as its name indicates, includes the illegal trading by the corporate insiders such as directors, managers, officers, and employees. Modern insider trading law expanded the scope of the potential violators to outsider traders who receive inside information from the corporate insiders. In analyzing SEC enforcement in insider trading cases, this research first examines the backgrounds of the defendants to see what kind of people are more frequently involved in the insider trading enforcement actions.

The defendants in this survey are categorized into five different types. “Corporate Insider” represents traditional corporate insiders, such as board of directors, officers/managers, and employees of the company. “Quasi-insider” includes attorneys, accountants, and those who gain access to the inside information occasionally with the permission of the company. Quasi-insiders sometimes are referred as “temporary insiders”. “Financial Professional” represents members of the securities or investment industry, such as broker-dealer, portfolio managers, and analysts. “Company” represents the companies which trade on its own securities and are listed as defendants. “Others” represents

---

76 CHOI & PRITCHARD, supra note 1, at 384. In United States v. O’Hagan, the Supreme Court validated the misappropriation theory which addressed the liability of traders who breach the fiduciary duty to or “misappropriate” from the source of the information. Id. at 384-86.
defendants who do not belong to any of the four categories mentioned above. Family members and friends of any person listed above are also included in each respective category. For example, when a wife of a director trades with inside information she learned from her husband, the wife is counted as a corporate insider.\(^\text{77}\)

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of Actions</td>
<td>37</td>
<td>53</td>
<td>57</td>
<td>58</td>
</tr>
<tr>
<td>Corporate Insider</td>
<td>18</td>
<td>24</td>
<td>24</td>
<td>31</td>
</tr>
<tr>
<td>Quasi-insider</td>
<td>8</td>
<td>11</td>
<td>12</td>
<td>16</td>
</tr>
<tr>
<td>Financial Professional</td>
<td>11</td>
<td>22</td>
<td>20</td>
<td>15</td>
</tr>
<tr>
<td>Company</td>
<td>0</td>
<td>0</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Others</td>
<td>1</td>
<td>1</td>
<td>6</td>
<td>3</td>
</tr>
</tbody>
</table>

*Table 3: Defendant Type—2009 to 2012*

As one can observe from the table above, corporate insiders are still the main source of violations, or at least are the main targets of investigation. Financial professionals also play an important role in trading with illegal inside information. (most importantly *SEC v. Galleon Management, LP, et al.* (2010) and *SEC v. Mark Anthony Longoria et al.* (2011). The former involved twenty-one defendants in civil proceedings and eleven defendants in parallel criminal proceedings, as the latter involved eleven in civil and right in criminal proceedings). Also, tipping close friends or family members is common across all categories of defendants.

We then examine the types of information being used or misappropriated. This analysis reveals the types of information that often triggers insider trading. Or alternatively, it reveals the focus of the SEC’s investigation but not necessarily the whole picture of the world of insider trading activities. To be sure, mergers and related events are inherently sensitive and constitute the majority of federal securities violation investigations. Accordingly, from the company side, relevant information needs to be handled with extreme care to prevent insider trading.

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>M&amp;A and Other Major Transactions</td>
<td>27</td>
<td>30</td>
<td>45</td>
<td>45</td>
</tr>
<tr>
<td>Earnings &amp; Financial Reports</td>
<td>3</td>
<td>11</td>
<td>8</td>
<td>9</td>
</tr>
<tr>
<td>Capital Related (e.g., Large New Stock Issuance)</td>
<td>3</td>
<td>0</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Major Events Regarding Business Operation</td>
<td>4</td>
<td>8</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>Other</td>
<td>2</td>
<td>6</td>
<td>1</td>
<td>1</td>
</tr>
</tbody>
</table>

*Table 4: Types of Information Used in Insider Trading Cases—2009 to 2012*

\(^\text{77}\) When an enforcement action includes more than one type of defendant, our data records each category respectively. For example, if in a case a corporate insider tipped a financial analyst about a pending acquisition that is about to go through, and then later on they both trade on that information, we record once in both the “corporate insider” and “financial professional” column. Also, even if there are multiple corporate insider trade with inside information, we only count once in the column of “corporate insider.”
3.1.4  Case Results and Illicit Gain

The handlings, and their results, are the core of any legal action. As repeatedly seen, various literatures and observations emphasize that most of the SEC’s enforcement action end up with settlement. We first summarize the results of action in the following table and confirm that observation with calculated numbers.

<table>
<thead>
<tr>
<th>Case Result</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Settled</td>
<td>30</td>
<td>42</td>
<td>38</td>
<td>38</td>
<td>148</td>
</tr>
<tr>
<td>Court Decided without Settlement</td>
<td>4</td>
<td>4</td>
<td>9</td>
<td>10</td>
<td>27</td>
</tr>
<tr>
<td>Only Some Defendants Settled</td>
<td>2</td>
<td>6</td>
<td>5</td>
<td>6</td>
<td>19</td>
</tr>
<tr>
<td>Data Not Available</td>
<td>1</td>
<td>1</td>
<td>5</td>
<td>4</td>
<td>11</td>
</tr>
<tr>
<td><strong>Settled Cases to All Cases with Relevant Information</strong></td>
<td>83%</td>
<td>81%</td>
<td>73%</td>
<td>70%</td>
<td>72%</td>
</tr>
</tbody>
</table>

*Table 5: Results of Action—2009 to 2012*

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th></th>
<th>2012</th>
<th>total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Number of Defendants</td>
<td>78</td>
<td>119</td>
<td>106</td>
<td></td>
<td>120</td>
<td>423</td>
</tr>
<tr>
<td>Number of Settled Defendants</td>
<td>57</td>
<td>97</td>
<td>80</td>
<td></td>
<td>76</td>
<td>310</td>
</tr>
<tr>
<td>Settlement Ratio</td>
<td>73%</td>
<td>81%</td>
<td>75%</td>
<td></td>
<td>63%</td>
<td>73%</td>
</tr>
</tbody>
</table>

*Table 6: Number of Settled Defendants & Settlement Rates (2009~2012)*

Illicit gain is another focal point to understand the whole picture of U.S. insider trading law enforcement. From the table below, we learn that cases with illegal gain of more than one million range from 9% to 30% in our survey period. Put differently, large scale insider trading is sporadic if not seldom. But it still unable to say with certainty if this result comes from a successful enforcement, or oppositely from a lax enforcement which cannot detect large scale violation effectively. But large numbers of small violations can logically be linked to a higher settlement rate.

<table>
<thead>
<tr>
<th></th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cases with Relevant Info</td>
<td>26</td>
<td>30</td>
<td>45</td>
<td>43</td>
<td></td>
</tr>
<tr>
<td>Less or Equal to $100,000</td>
<td>9</td>
<td>10</td>
<td>17</td>
<td>24</td>
<td></td>
</tr>
<tr>
<td>$100,001~$1,000,000</td>
<td>12</td>
<td>11</td>
<td>18</td>
<td>15</td>
<td></td>
</tr>
<tr>
<td>Over $1,000,000</td>
<td>5</td>
<td>9</td>
<td>10</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Over $1,000,000 Cases to All</td>
<td>19%</td>
<td>30%</td>
<td>22%</td>
<td>9%</td>
<td></td>
</tr>
</tbody>
</table>

*Table 7: Illicit Gain—2009 to 2012 (Unit: Case. The Total of All Defendants)*

---

78 We calculate partial settlement as zero in this column.

79 This number excludes relief defendants.
3.1.5 Penalties and Settlements

Civil proceedings triggered by the SEC often lead to multiple sanctions, including monetary and non-monetary penalties. We first put together the civil penalties applied that we collect from the data.

<table>
<thead>
<tr>
<th>Cases with Relevant Info</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less or Equal to $100,000</td>
<td>12</td>
<td>15</td>
<td>14</td>
<td>23</td>
</tr>
<tr>
<td>$100,001~$1,000,000</td>
<td>9</td>
<td>5</td>
<td>5</td>
<td>8</td>
</tr>
<tr>
<td>Over $1,000,000</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

*Table 8: Civil Penalty—2009 to 2012 (All penalties from each defendant in a case are added up together)*

We then compare the civil penalty to illicit gain to see the relationship. In the following table, we use each defendant as the unit to see the relationship between civil penalty to illicit gain in insider trading. Noticeably, the civil penalty received is usually equal or less than one time of the illicit gain, in addition to the disgorged gain. Two reasons might be implicated: one is nature of case as the cases SEC actually investigated are relatively small (see table 7); two is when in a settlement, usually SEC cannot have the legally highest penalty it can imposed, which is three-time of the illicit gain, as SEC has to concede to reach a settlement.

<table>
<thead>
<tr>
<th>Civil Penalties/Illicit Profits</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than one time</td>
<td>6</td>
<td>12</td>
<td>11</td>
<td>20</td>
</tr>
<tr>
<td>Equal to one time</td>
<td>19</td>
<td>11</td>
<td>18</td>
<td>29</td>
</tr>
<tr>
<td>Between one time and two times</td>
<td>1</td>
<td>1</td>
<td>6</td>
<td>4</td>
</tr>
<tr>
<td>Greater than two times</td>
<td>4</td>
<td>5</td>
<td>1</td>
<td>4</td>
</tr>
</tbody>
</table>

*Table 9: Relationship between Civil Penalties and Illicit Profits—2009 to 2012 (Number of Defendants)*

Beside monetary remedies, there are other types of remedies that the SEC could seek to meet its regulatory goal. Among them are permanent injunctions, director/manager bars, cease-and-desist orders, temporary orders and professional disciplines. The first two are available in civil actions which take place in the federal courts. The latter three are available in administrative proceedings supervised by an administrative law judge. This research identifies the use of those remedies for each case each year.

From our data, remedies other than monetary penalties play a more important role than was previously understood. The survey reveals heavy reliance on the permanent injunction in the SEC’s practice. This phenomenon echoes the link among the defendants’ occupational status, the access to material information, and the misuse of information for the purpose of illegal trading. Further, to some extent, the SEC seems to adapt the penalties to the harm done or potential threat posed to the calculation of sanctions.

<table>
<thead>
<tr>
<th>Remedy Types/Number of Issuance</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Permanent Injunction</td>
<td>55</td>
<td>83</td>
<td>77</td>
<td>76</td>
</tr>
<tr>
<td>Director/Manager Bar</td>
<td>3</td>
<td>6</td>
<td>6</td>
<td>15</td>
</tr>
<tr>
<td>Cease-and-Desist Order</td>
<td>0</td>
<td>3</td>
<td>0</td>
<td>1</td>
</tr>
</tbody>
</table>
We also document the amount of settlement in cases, which include disgorgement (illicit gain plus interest) and civil penalty, and summarize in the following table.

<table>
<thead>
<tr>
<th>Cases with Relevant Info</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less or Equal to $100,000</td>
<td>6</td>
<td>5</td>
<td>9</td>
<td>12</td>
</tr>
<tr>
<td>$100,001~$1,000,000</td>
<td>12</td>
<td>13</td>
<td>15</td>
<td>18</td>
</tr>
<tr>
<td>Over $1,000,000</td>
<td>4</td>
<td>8</td>
<td>7</td>
<td>6</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Total Number of Defendants in SEC Actions</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Defendants Involved in Parallel Criminal Actions</td>
<td>15</td>
<td>37</td>
<td>30</td>
<td>15</td>
</tr>
<tr>
<td>Civil Cases involving Parallel Criminal Action</td>
<td>5</td>
<td>17</td>
<td>16</td>
<td>13</td>
</tr>
</tbody>
</table>

3.1.6 Parallel Criminal Charges

As mentioned, the SEC has continued to refer willful violations of the securities laws to the Department of Justice for criminal prosecution when a violation is substantial, and it is generally considered to be a powerful weapon to fight against large scale violations. It is thus useful to look at the number of parallel criminal actions of the insider trading cases each year. Our survey shows the cases that actually go to criminal proceeding are less than what is earlier expected. The higher standard of proof in criminal proceeding and the secrecy nature in insider trading activities may explain part of the phenomenon. For the details of all criminal proceedings, please see appendix 2.

<table>
<thead>
<tr>
<th>Time Span from Behavior Date until SEC File Charges</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 to 12 months</td>
<td>11</td>
<td>16</td>
</tr>
<tr>
<td>12 to 36 months</td>
<td>41</td>
<td>37</td>
</tr>
<tr>
<td>36 to 60 months</td>
<td>36</td>
<td>52</td>
</tr>
<tr>
<td>Over 60 months</td>
<td>9</td>
<td>8</td>
</tr>
</tbody>
</table>

3.1.7 Time Duration

In this section, the dates of violation, the SEC filing date, and the closing date of cases are examined. By looking at this data, the length of time for the enforcement staff to investigate or resolve an insider trading can be observed, which can make an inference on the SEC’s efficiency.
### Table 14: Time Span from SEC File Charges Until Settlement or Final Judgment Date — 2011 to 2012

<table>
<thead>
<tr>
<th>Time Span from SEC File Charges Until Settlement or Final Judgment Date</th>
<th>Number of Defendants</th>
</tr>
</thead>
<tbody>
<tr>
<td>0 to 3 months</td>
<td>22</td>
</tr>
<tr>
<td>3 to 12 months</td>
<td>34</td>
</tr>
<tr>
<td>Over 12 months</td>
<td>18</td>
</tr>
</tbody>
</table>

### Table 15: Average Time Span — 2011 to 2012

<table>
<thead>
<tr>
<th>Time Span From Behavior Starts Date Until SEC File Charges</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>34.8</td>
<td>35.2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Time Span From SEC File Charges Until Settlement or Final Judgment Date</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>8.0</td>
<td>4.49</td>
</tr>
</tbody>
</table>

### 3.1.8 Additional Database Results

To help compare our surveyed result with other surveys, we add enforcement actions data compiled by the SEC before the FY2009 below to improve understanding.

### Table 16: Insider Trading Enforcement Actions by SEC — 2005 to 2008

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Insider Trading Enforcement Actions</td>
<td>50</td>
<td>46</td>
<td>47</td>
<td>61</td>
</tr>
<tr>
<td>Total SEC enforcement Actions</td>
<td>630</td>
<td>574</td>
<td>656</td>
<td>671</td>
</tr>
<tr>
<td>% of total action</td>
<td>8%</td>
<td>8%</td>
<td>7%</td>
<td>9%</td>
</tr>
</tbody>
</table>

*Source: Selected SEC and Market Data (2005~2008)*

In addition, we use NERA long-term data for further reference. NERA, a private economic consulting company focusing on applying quantitative data for legal and business analysis, regularly follows SEC settlement trends and class actions and publishes their results for clients and the public. According to NERA’s SEC Settlement Trends: 2H12 Update, we can have insider trading settlement cases statistics in the last decade. The difference between NERA and our survey is also listed below.

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual</td>
<td>99</td>
<td>68</td>
<td>93</td>
<td>72</td>
<td>60</td>
<td>74</td>
<td>56</td>
<td>69</td>
<td>63</td>
<td>118</td>
</tr>
<tr>
<td>Companies</td>
<td>5</td>
<td>2</td>
<td>3</td>
<td>6</td>
<td>7</td>
<td>2</td>
<td>10</td>
<td>4</td>
<td>5</td>
<td>8</td>
</tr>
</tbody>
</table>

---

<table>
<thead>
<tr>
<th>Total</th>
<th>104</th>
<th>70</th>
<th>96</th>
<th>78</th>
<th>67</th>
<th>76</th>
<th>66</th>
<th>73</th>
<th>68</th>
<th>126</th>
</tr>
</thead>
</table>

**Table 17: SEC’s Settlement in Insider Trading—Number of Settlements for Individuals Reached, compiled by NERA Economic Consulting**

*Source: NERA Economic Consulting, SEC Settlement Trends: 2H12 Update*

<table>
<thead>
<tr>
<th>Number of Settled Defendants</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>total</th>
</tr>
</thead>
<tbody>
<tr>
<td>NERA’s</td>
<td>66</td>
<td>73</td>
<td>68</td>
<td>126</td>
<td>333</td>
</tr>
<tr>
<td>Our Survey</td>
<td>57</td>
<td>97</td>
<td>80</td>
<td>76</td>
<td>310</td>
</tr>
</tbody>
</table>

**Table 18: Comparison of Settlement Surveys: NERA and Our Survey—2009 to 2012**

Basically, two survey results apply the same method (collecting data from SEC’s litigation release). Still, we record the year of settlement in the year when the case was filed. However, the settlement date may come later in the next year. The other survey records the year when it is settled, not filed. This partly explains the difference between two surveys when period-to-period comparison is conducted.

3.2 Role of Settlement in SEC’s Insider Trading Cases

As noted earlier, the SEC’s enforcement actions usually ended with settlements. Settlement often appears in the form of a consent order in an administrative proceeding (under section 21C or 15(c)(4)) or a consent decree in district court by which the Commission approves. In general, targets of investigation settle his/her cases to avoid the cost of litigation and seek a less severe penalty when evidence presented constitutes a solid preponderance.

3.2.1 Why Settling a Case?

For the SEC, a negotiated settlement provides a needed incentive for targets of investigation to cooperate, and co-operation from targets eventually reduces the burden of investigation and contributes to better efficiency in investigation. The extensive use of settlement in fact allows the SEC to handle more cases as less need to go to court or go through the final stage of proceeding. For respondents, settlement is also a good thing as the penalty tends to

---


82 Scholars observe “most investigations are concluded by a settlement after the (SEC) staff’s informal investigation.” CHOI & PRITCHARD, *supra* note 1, at 196. See also, COX ET AL., *supra* note 47, at 806 (Most SEC enforcement proceedings (over 90 percent) are settled, not litigated). Similar observation can be found in scholarly work in the 1980s and 1990s. See Committee on Federal Regulation of Securities, *Report of the Task Force on SEC Settlements*, 47 BUS. LAW. 1083, 1104 (1992) (“As is the case with judicial proceedings, the majority of administrative proceedings traditionally are settled prior to any evidential hearing or other adjudication of any matter of fact or issue of law”).

83 SEC ENFORCEMENT MANUAL § 6.

84 For example, according to an earlier report, averages around 600 or 700 actions were brought by the SEC annually in the years previous to 2007. *Proceedings of the 2007 Midwest Securities Law Institute*, 8 J. BUS. & SEC. L. 59, 98 (2007). A caseload of such magnitude requires speedier handling which presses more settlements from the SEC’s side.
be lighter as well as allowing respondents the opportunity to take part in the decision and prepare for it. Based on the factors listed, settlements are reached more often than much of the other regulatory field.

Prof. Stephen Choi and A.C. Pritchard in their casebook also list four costs that targets want to avoid by settling their case: (1) the continuing harm to their reputation; (2) the enormous litigation cost against federal government; (3) a referral to the Department of Justice for possible criminal prosecution, and (4) the ruinous potential private liability that could come from the collateral estoppels effect of an adverse judgment. Similar observations can also be found in other literature.

The extensive use of settlement reflects several factual assumptions, which mainly include (a) high litigation cost; (b) severe punishment looming (compared to a settled result, if defendant loses the case); and (c) high possibility that the SEC can win in its case. These three factors largely mutually exist as both the SEC and defendants are aware of and agree on the existence of these assumptions.

3.2.2 Factors of Consideration from the SEC Side

As Enforcement Manual indicates, SEC listed four evaluations in striking a settlement:

a. The assistance provided by the cooperating individual in the Commission’s investigation or related enforcement actions;
b. The importance of the underlying matter in which the individual cooperated;
c. The societal interest in ensuring that the cooperating individual is held accountable for his or her misconduct; and

d. The appropriateness of cooperation credit based upon the profile of the cooperating individual.

For the SEC, most importantly, the decision to settle with the targets of investigation is based on the premise that the settlement already represents a sufficient punishment for the harm that the violation caused, and also constitutes enough deterrence for potential future violation, especially in light of the gravity of violations and the cost calculation to the SEC if the legal proceeding continues. In the meantime, the SEC still litigates the cases it deems necessary to vindicate important legal principles.

---

85 CHOI & PRITCHARD, supra note 1, at 191. Similar observation, see COX ET AL., supra note 47, at 807.


87 One SEC officer in a conference discussion cited the success rate of the SEC in administrative proceeding ranged between 72% and 92% from 2003 to 2007. Proceedings of the 2007 Midwest Securities Law Institute Symposium, supra note 84, at 98 (Comment from an SEC branch officer).

88 17 C.F.R. § 202.12. See also SEC ENFORCEMENT MANUAL § 6.1.1.

89 Committee on Federal Regulation of Securities, supra note 86, at 1093.
3.2.3 Criticism

The use of settlement in securities law violation, especially in insider trading cases, is also facing several strong challenges. The first criticism concerns the very idea of holding the violation less than fully accountable. There is a tension between punishing violations to its full extent and providing incentive to allow cooperation, and this tension consistently exists by the nature of settlement. Similarly, by the same token, the use of settlement conceptually blurs the line between the means and end.

Second, in terms of the actual determination of a settlement, the trade-off between assistance and reduced penalty may be distorted and hard to assess. It is hard to know if a settlement systematically goes too lightly or conversely imposes severe penalty or even any penalty in a hard-to-win case. In the worst case scenario, this distortion can go both ways in the same case. The assessment problem becomes even more obvious when a judicial review of a settlement is absent or carried out without full disclosure of relevant facts and evidences. But ironically, a too-detailed fact-finding and judicial review works against cost reduction—the exact idea to have a settlement in the first place.

Last, the different bargaining power of each respondent complicates the settlement result. By the method that settlements operate, the more powerful or rich targets are inclined to gets lighter sanctions. This result works right against the starting point to punish white-collar crime, which should be class-sensitive in an opposite direction.

3.2.4 Reflection

Clearly, like many things, powerful criticisms also need factual support. A long-term comparison provides a more complete picture in this regard. In a report of 1992 on the SEC’s settlement practice by a task force (appointed by the Subcommittee on Civil Litigation and SEC Enforcement Matters of the Federal Regulation of Securities Committee of the American Bar Association's Section of Business Law), several useful background understandings are provided. According to that report, in fiscal year 1990, the SEC received about 52,000 investor complaints and inquiries, a 290% increase over FY 1982, 1,218 Matters Under Inquiry (“MUI's”) were opened, which is approximately 30% more than the number in FY 1987. Further, the SEC opened 362 new investigations in FY 1990, bringing the total number of pending SEC investigations to 1,152, and the average life of an investigation is two years and four months, representing an increase by nearly 17% from 1987.

---

90 17 C.F.R. § 202.12. See also SEC ENFORCEMENT MANUAL § 6.1.1.

91 In addition, there are criticisms arguing that the SEC’s settlements may imply too many concerns from the SEC’s own perspective and there might be a potential conflict of its own interest within. See e.g., Danne L. Johnson, SEC Settlement: Agency Self-interest or Public Interest, 12 FORDHAM J. CORP. & FIN. L. 627 (2007)(Arguing the inherent self-interest problem in the SEC’s settlement and advocating to re-focus on the public interest aspect in the SEC’s decision).

92 Committee on Federal Regulation of Securities, supra note 86, at 1095.

93 Id.

94 Id.

95 Id.
Two things can be inferred from the analysis above. First, compared to the number of complaints and MUIs, discretion and differential treatments should be allowed, which can theoretically improve the securities agency’s ability to deal with its increasing caseload. Second, the fundamental issue of whether settlements can be trusted lies on the quality of the SEC’s decision in various cases. To be specific, the use of settlement can be beneficial if (and only if) the SEC constantly decides cases wisely. In this sense, the desirability and merit of extensive use of settlement is more of a function of several factual settings, including the quality and effectiveness of the securities agency’s investigation and assessment, and the caseloads it has to deal with, but not a clear-cut right-or-wrong answer which can be deducted from pure theory.\textsuperscript{96}

3.3 Parallel Criminal Investigation and Optimality of Punishments

3.3.1 The Optimal Punishment in Securities Law

As noted, criminal sanction is available for conduct violating the prohibition against insider trading.\textsuperscript{97} In practice, criminal sanction plays an essential role in securities law in deterring hard-core fraudsters.\textsuperscript{98} But whether or to what extent the division of labor between civil and criminal proceeding is justified, or desirable, in terms of preventing securities fraud and insider trading, is still an issue of debate among academics. Interestingly, opposed to the criticism arguing against settlement due to the reduced penalty, many criminal law scholars question the very use of criminal law in white-collar crime and its effects.\textsuperscript{99} The polarized opinions distinctly point to the fact of how sensitive an issue it is to use criminal sanction in punishing securities law violations, especially activities such as insider trading.

3.3.2 Parallel Proceedings and Its Problems

Beyond the theoretical debate about the merit of using criminal sanction in insider trading cases, the fact that agencies (SEC and DOJ) coordinate their investigations, share investigation products, and use civil and paralleling criminal prosecution creates issues to be addressed.

First is about the concern of whether piling proceedings constitute double jeopardy. In theory, when civil penalty crosses a certain level and becomes punitive in nature, it could constitute punishment that falls within the meaning of

---

\textsuperscript{96} Therefore, from a comparative perspective, whether a country is suitable for a more extensive use of settlement for securities law violations in fact depends on the quality of the securities agency. In particular, the professionalism and independence are essential in managing a trustworthy settlement mechanism.

\textsuperscript{97} See supra 2.2.3.

\textsuperscript{98} CHOI & PRITCHARD, supra note 1, at 230.

the Double Jeopardy Clause of the Constitution.\textsuperscript{100} However, in an important case \textit{Hudson v. United States},\textsuperscript{101} the Supreme Court visited this issue and ruled that when Congress clearly designates the sanctions of a money penalty in statutes as “civil,” the sanctions are not punitive and thus no double jeopardy applied to bar criminal prosecution.\textsuperscript{102} Following the same reasoning, in a more recent case \textit{United States v. Van Waeyenberghe},\textsuperscript{103} which directly involved the SEC’s civil action and later criminal charges, Second Circuit clearly affirmed criminal conviction by lower court and rejected the double jeopardy defense. In short, without clearest proof suggesting that the sanctions were so punitive in form and effect as to render them criminal, Congress’ intent and designation should be followed.\textsuperscript{104} That is to say, in dealing with securities law violations, SEC civil proceeding and DOJ’s criminal proceeding are different in its legal nature and thus no double jeopardy is implied thereof.

Second issue concerns the application of Fifth Amendment privilege when multiple proceedings are looming. As commonly known, in criminal procedure defendants enjoy the Fifth Amendment rights, such as privilege against self-incrimination. But whether a target can or should be allowed to assert the Fifth Amendment privilege in the SEC’s civil proceeding becomes a problem, especially when the SEC reserves the right to refer the case to the DOJ and might share its investigation products with the DOJ if it decides so. One example is the use the subpoenas by the SEC has mandatory power backed by contempt of court.\textsuperscript{105} In this instance, whether the SEC’s subpoena power endangers potential defendant’s Fifth Amendment right against self-incrimination becomes obvious.

To deal with these problems, at least partly, the SEC adopts a middle-ground strategy in its Rule of Practice, which provides sort of quasi-criminal procedural protection to the targets of its investigation so that those investigation products can be also used in a criminal proceeding to avoid redundancy or overlapping. For example, in formal investigation, a witness can be compelled to furnish documents or testify,\textsuperscript{106} has the right to counsel,\textsuperscript{107} and a

\textsuperscript{100} In the context of Civil False Claim Act, an important Supreme Court decision \textit{United States v. Halper} found that when a civil penalty is so unrelated to the remedial goals of the statute that it constitutes punishment within the meaning of the Double Jeopardy Clause of the Constitution. United States v. Halper, 90 U.S. 435 (1989).

\textsuperscript{101} 522 U.S. 93 (1997).

\textsuperscript{102} \textit{Id.} at 94. In \textit{Hudson}, Supreme Court cites the test in \textit{United States v. Ward} and \textit{Kennedy v. Mendoza-Martinez} and listed factors to consider in determining whether sanctions are punitive. These factors include: (1) “[w]hether the sanction involves an affirmative disability or restraint”; (2) “whether it has historically been regarded as a punishment”; (3) “whether it comes into play only on a finding of scienter”; (4) “whether its operation will promote the traditional aims of punishment-retribution and deterrence”; (5) “whether the behavior to which it applies is already a crime”; (6) “whether an alternative purpose to which it may rationally be connected is assignable for it”; and (7) “whether it appears *100 excessive in relation to the alternative purpose assigned.” It is important to note, however, that “these factors must be considered in relation to the statute on its face.” \textit{Id.} at 99-100.

\textsuperscript{103} 481 F.3d 951 (7th Cir.2007).

\textsuperscript{104} 522 U.S. 93, 94 (1997).

\textsuperscript{105} \textit{CHOI & PRITCHARD, supra} note 1, at 197.

\textsuperscript{106} 17 C.F.R. § 203.7(a), (b).

\textsuperscript{107} 17 C.F.R. § 203.7(c).
reasonable opportunity of cross-examination and production of rebuttal testimony or documentary evidence if the record shall contain implications of wrongdoing of his.\footnote{108} In this regard, testimony from a SEC investigation, where witnesses need to be sworn,\footnote{109} can be used in a criminal case. Further, targets of investigation in the SEC’s civil proceeding still can assert the privilege against self-incrimination in response to SEC inquiries and refuse to answer.\footnote{110} However, as scholars clearly point out, this assertion might lead to an adverse inference which can be drawn against the target by the SEC if it is actually asserted.\footnote{111}

However, the reality of sharing information and investigation products does pose risk of using evidence obtained from a civil proceeding in a criminal case, which is likely to weaken a defendant’s right as the procedural protections in civil proceeding might be less.\footnote{112} In this regard, the SEC typically stays its action until the criminal case is resolved to avoid redundant investigation, and the stay is subject to the SEC’s discretion and with the consent of the court.\footnote{113} Also, if so, the SEC can wait until the conviction of criminal procedure and use collateral estoppels for an easy win.\footnote{114} But it is noteworthy that findings in a civil case cannot have a collateral estoppels effect in subsequent criminal proceedings, because criminal proceedings apply beyond a reasonable doubt as standard of guilt.\footnote{115}

\section*{4 Conclusion}
Fighting securities law violations is a difficult challenge, especially in an ever-changing market combining new technology and old desire. Limited resources become obvious in light of the growing size of markets. Therefore, a flexible and efficient enforcement mechanism turns into a starting point to conceive an answer to all related challenges.

\footnotetext[108]{17 C.F.R. § 203.7(d).} \footnotetext[109]{17 C.F.R. § 203.4(a).} \footnotetext[110]{CHOI & PRITCHARD, supra note 1, at 200.} \footnotetext[111]{Id.} \footnotetext[112]{In fact, in SEC v. Dresser Industries, Inc., 628 F.2d 1368 (D.C. Cir.), \textit{cert. denied}, 449 U.S. 993 (1980), court clearly pointed out the problems of having two parallel proceedings if a civil proceeding is not deferred (“The noncriminal proceeding, if not deferred, might undermine the party's Fifth Amendment privilege against self-incrimination, expand rights of criminal discovery beyond the limits of Federal Rule of Criminal Procedure 16(b), expose the basis of the defense to the prosecution in advance of criminal trial, or otherwise prejudice the case.”). \textit{Id.} at 1376. Court also considered a delay of the noncriminal proceeding would be justified if a delay does not seriously injure the public interest, but as no strong support is shown in the current case, the SEC’s administrative proceeding does not have to stay. \textit{Id.}} \footnotetext[113]{CHOI & PRITCHARD, supra note 1, at 207. \textit{See also} Seymour Glanzer \textit{et al., The Use of the Fifth Amendment in SEC Investigations}, 41 WASH. & LEE L. REV. 895, 920 (1984).} \footnotetext[114]{HAZEN, supra note 20, § 16.2[8].} \footnotetext[115]{Id.}
Experience from the United States and its long, formidable Securities and Exchange Commission thus becomes an important example to look into. Under the words and publicity, this Article examines the SEC’s enforcement actions by collecting its enforcement data during 2009 to 2012 litigation releases. By this means, nuances in individual cases and a more complete picture of insider trading violation enforcement in the United States comes clear along the way, and the need for, as well as the premise of, a workable layered enforcement mechanism and its legal issues are similarly discussed to provide a valuable lesson for similar-situated countries.