1997

Statutory Findings and Insider Trading Regulation

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Steve Thel, Statutory Findings and Insider Trading Regulation, 50 Vand. L. Rev. 1091 (1997)
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Statutory Findings and Insider Trading Regulation

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* Professor, Fordham University School of Law. I am grateful to Marc Arkin, Steve Bainbridge, Jim Brudney, Victor Brudney, Perry Dane, Jill Fisch, Martin Flaherty, Phil Frickey, Don Langevoort, Mark Patterson and Adam Pritchard for their help with this Article.

This Article was substantially complete when the Supreme Court granted certiorari in United States v. O'Hagan, 1997 U.S. LEXIS 4033 (June 25, 1997), which is discussed herein. I participated in the preparation of an amicus brief supporting the government in that case, filed on behalf of the North American Securities Administrators' Association, Inc., and a group of law professors. The statutory findings discussed in this Article were also discussed in that brief.

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I. INTRODUCTION

Insider trading has presented some of the most unsettled and contentious issues of corporate law. These issues have been particularly difficult because often it has not even been clear whether the law forbids those who possess material nonpublic information to trade securities. Even as commentators have debated whether insider trading ought to be forbidden, the courts have disagreed on the more basic question of when and whether such trading is, in fact, forbidden.1

The law governing insider trading has been unclear because the scope of the SEC’s authority to regulate insider trading has been unclear. For a while, courts uniformly held that section 10(b) of the Securities Exchange Act2 (the “Exchange Act”) authorizes the SEC to forbid trading by those in possession of misappropriated material nonpublic information, and that section 14(e) of the Exchange Act3 authorizes the Commission to forbid trading on the basis of any material nonpublic information about tender offers.4 However, two circuit courts of appeal subsequently rejected this precedent and held that the Commission could not forbid trading on the basis of misappropriated information or prohibit informed trading in the context of tender offers.5 Earlier this year, in United States v. O’Hagan,6 the Supreme Court held that (1) a person who trades securities for personal profit using confidential information misappropriated in breach of a fiduciary duty to the source of the information violates section 10(b) and rule 10b-5,7 and (2) at least insofar as the question had been presented to the Court, the SEC did

3. Id. § 78n(e).
4. See Part II.B (showing that section 14(e) allows the SEC to adopt a rule prohibiting trading while in possession of material nonpublic information dealing with tender offers). Another question is whether the prohibitions against insider trading come into play only when nonpublic information motivates the trade—that is, the trader trades on the basis of the information—or whether it is enough that the trader possesses such information. See Langevoort, Insider Trading § 3.04 (cited in note 1) (discussing whether motivation is relevant to insider training analysis). I take no position on that question here.
not exceed its rulemaking authority under section 14(e) when it adopted rule 14e-3, which establishes a sort of parity-of-information regime for trading in connection with tender offers.

Although the Court's opinion in *O'Hagan* strongly endorsed the SEC's regulation of insider trading, it left several important questions unanswered. For example, it is not entirely clear what sort of confidential relationship creates a duty of loyalty protected by section 10(b). Defendants presumably will argue that the breach of a noncommercial confidential relationship, such as that between a therapist and patient or between family members, does not suffice to establish securities fraud. In addition, the Court explicitly refrained from deciding whether rule 14e-3 is valid insofar as it prohibits trading in advance of a tender offer. A final question is whether the Court's holding was correct. Two courts of appeal had construed section 10(b) and rule 14e-3 much more narrowly, as had numerous academic commentators. Moreover, three justices dissented from parts of the majority's opinion in *O'Hagan*, and Justice Thomas, joined by the Chief Justice, strenuously argued that neither the misappropriation theory nor rule 14e-3 was consistent with the Exchange Act.

This Article is about a provision of the Insider Trading and Securities Fraud Enforcement Act of 1988 ("the 1988 Act") that directly addressed the validity of rule 14e-3 and the misappropriation doctrine, and the parameters of the latter. In the 1988 Act, Congress declared its finding that the "rules and regulations of the Securities and Exchange Commission under the Securities Exchange Act of 1934 . . . governing trading while in possession of material, nonpublic information are, as required by such Act, necessary and appropriate in the public interest and for the protection of investors." The statute further provided that the SEC had "enforced such rules and regulations vigorously, effectively, and fairly."

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8. Id. § 240.14e-3.
9. See 1997 U.S. LEXIS 4033 at *31. The Court stated:
   The [misappropriation] theory is . . . well-tuned to an animating purpose of the Exchange Act: to insure honest securities markets and thereby promote investor confidence . . . . Although informational disparity is inevitable in the securities markets, investors likely would hesitate to venture their capital in a market where trading based on misappropriated nonpublic information is unchecked by law. An investor's informational disadvantage vis-à-vis a misappropriator with material, nonpublic information stems from contrivance, not luck; it is a disadvantage that cannot be overcome with research or skill.
Inasmuch as the Exchange Act authorizes the SEC to promulgate necessary and appropriate rules and the 1988 Act says that the SEC's insider trading rules are necessary and appropriate, on first reading these findings seem to settle the matter and establish that the SEC's insider trading initiatives are within its statutory authority. Surprisingly, however, they have not figured at all in the debate over the validity of the SEC rules. Thus, one purpose of this Article is simply to highlight their existence.

If everyone has ignored a nine-year-old statute that purported to establish the validity of the rules against insider trading, one might wonder whether the findings really established their validity. As a practical matter, they did not, for the validity of the SEC's rulemaking initiatives remained in doubt after the statute was enacted, and the courts that addressed their legitimacy essentially ignored the 1988 Act's findings. The Supreme Court noted the existence of the findings in O'Hagan, but since it upheld the misappropriation theory and rule 14e-3 on the basis of sections 10(b) and 14(e), the Court chose not to discuss the 1988 Act. Inasmuch as the Court's holding is largely consistent with the dictates of the 1988 Act, this omission may have been of little moment, and perhaps the findings influenced the ultimate decisions of the majority. However, the same cannot be said of the lower courts that rejected the misappropriation theory and rule 14e-3 without mentioning the findings, nor of the dissenting Justices in O'Hagan, who did not mention the findings.

The other purpose of this Article is to identify the implications of the 1988 Act for the law of insider trading, and, more generally, to

12. In O'Hagan, the Supreme Court noted that the government argued that Congress confirmed the validity of the misappropriation theory and rule 14e-3 in these findings. 1997 U.S. LEXIS 4033 at n.11. However, the Court explained that it did not address the 1988 Act since it upheld the misappropriation theory and rule 14e-3 on the basis of sections 10(b) and 14(e). Id. at n.22. The dissenting opinions did not mention the findings. I am not aware of any extended discussion of the findings. The only other published references to these findings outside of the 1988 Act and its legislative history seem to be in SEC v. Peters, 978 F.2d 1162, 1167 (10th Cir. 1992), and in a few law review articles. In Peters, which arose before the findings were enacted, the court said that the findings supported its holding that rule 14e-3 was valid. Id. The articles each mention the findings briefly and all suggest that they indicated congressional support or ratification of the misappropriation doctrine and/or rule 14e-3. See Stephen M. Bainbridge, Incorporating State Law Fiduciary Duties into the Federal Insider Trading Prohibition, 52 Wash. & Lee L. Rev. 1189, 1232-33 (1996); Howard M. Friedman, The Insider Trading and Securities Fraud Enforcement Act of 1988, 68 N.C. L. Rev. 455, 474-75 (1990); Stuart J. Kaswell, An Insider's View of the Insider Trading and Securities Fraud Enforcement Act of 1988, 45 Bus. Law. 146, 167-88 (1989); Steve Thel, The Genesis of Section 16: Regulating the Management of Publicly Held Companies, 42 Hastings L. J. 391, 414 n.70 (1991); Steve Thel, The Original Conception of Section 10(b) of the Securities Exchange Act, 42 Stan. L. Rev. 385, 464 n.362 (1990); Steve Thel, Section 20(d) of the Securities Exchange Act, 69 N.C. L. Rev. 1261, 1268 (1991).

begin to explore the use of statutory law finding as a technique for establishing substantive law. Given the heat of the debate over how much power Congress has given the SEC to regulate insider trading, it is remarkable that a statute directly addressed to that issue has been ignored for all practical purposes. Part of the explanation no doubt lies in the fact that the relevant portions of the 1988 Act are hard to find. Yet given the high stakes involved in insider trading litigation, the statute should have at least been considered. The fuller explanation is probably that courts and lawyers are used to treating insider trading law as common law, even though courts regularly rebuff SEC initiatives by incanting that if law is to be made, Congress has to do it. Perhaps, for securities regulation at least, what is needed is a better law of statutes for an age of common law.

This Article begins by outlining the extra-legislative development of insider trading law over the last two decades. After noting the restrictions on the SEC's regulatory power established by the Supreme Court in the early 1980s, Part II turns to the SEC's initially

14. The findings are not included as a numbered section of the United States Code, (although they are appended to 15 U.S.C. § 78u-1 (1994)), nor are they included in the various single-volume collections of federal securities statutes and rules. Title 15 of the United States Code has not been enacted into law, but is merely a compilation of statutes, including the 1988 Act.

15. See United States v. Chestman, 947 F.2d 551, 572 (2d Cir. 1991) (en banc) (Winter, J., concurring in part and dissenting in part) ("The legal rules governing insider trading under Section 10(b) are based solely on administrative and judicial case law.").

16. See Dirks v. SEC, 463 U.S. 646, 656-58 (1983) (rejecting the SEC's theory of tippee liability as inconsistent with the Court's view of congressional intent in Chiarella v. United States, 445 U.S. 222 (1980)). See also O'Hagan, 1997 U.S. LEXIS 4033 at *82 (Thomas, J., dissenting) ("The repeated reliance on such broad-sweeping legislative purposes reaches too far and is misleading in the context of the misappropriation theory. It reaches too far in that, regardless of the overarching purpose of the securities laws, it is not illegal to run afoul of the 'purpose' of a statute, only its letter."); Central Bank, N.A. v. First Interstate Bank, N.A., 511 U.S. 164, 173 (1994) (stating that the statutory text controls the definition of conduct forbidden under § 10(b)); Chiarella, 445 U.S. at 234 ("The 1934 Act cannot be read more broadly than its language and the statutory scheme reasonably permit.") (quoting Touche Ross & Co. v. Redington, 442 U.S. 560, 578 (1979), which was quoting SEC v. Sloan, 436 U.S. 103, 116 (1978) (internal quotation marks omitted); Santa Fe Industries, Inc. v. Green, 430 U.S. 462, 472-73 (1977) (holding that the rulemaking power granted to the SEC is not the power to make law and therefore cannot exceed the power granted to it by Congress in § 10(b)) (citing and quoting Ernst & Ernst v. Hochfelder, 425 U.S. 185, 214 (1975)).

successful attempt to circumvent those restrictions with the misappropriation doctrine under rule 10b-5 and the parity-of-information regime it established for tender offers with rule 14e-3. The misappropriation doctrine and rule 14e-3 have both been controversial, and this outline is not intended to show they were either wise or within the Commission's authority. On the contrary, the point of this Article is that the findings were enacted precisely because the Commission's authority to enforce the misappropriation doctrine and rule 14e-3 had come into question by the time the 1988 Act was enacted. Part II concludes with a brief discussion of the judiciary's reaction to the misappropriation doctrine and rule 14e-3 since 1988, including recent decisions holding them to be beyond the SEC's authority. The purpose of this discussion is not to quarrel with these decisions or to establish the validity of the misappropriation doctrine and rule 14e-3—the Supreme Court's opinion in O'Hagan has established their validity, at least in broad outline. Instead, these decisions are discussed simply to show that the primary attack on the SEC's insider trading initiatives went to the scope of the Commission's power to regulate trading, and to highlight the issue that Congress faced when it addressed the validity of the Commission's initiatives in 1988.

Part III of this Article discusses the 1988 Act, particularly its declaration that rules 10b-5 and 14e-3 are valid to the extent that they forbid trading on the basis of material nonpublic information. Part IV examines implications of the 1988 Act's findings. These findings present complicated problems, and the question of whether the courts are bound to respect them turns largely on the way courts and Congress ought to interact. However, past judicial practice with respect to analogous statutes indicates that courts should respect the will of Congress expressed in the findings. In 1988, statutory findings were the best mechanism available for Congress to establish the enforceability of rule 14e-3 and the misappropriation doctrine. By ignoring those findings, the same courts that insisted that Congress ought to make securities law relegated Congress to a relatively insignificant lawmaking role in which it could not even make itself heard.
II. THE DEVELOPMENT OF THE MISAPPROPRIATION DOCTRINE AND RULE 14E-3

A. Insider Trading and Deception

The language of the Exchange Act has been the starting point for discussion of the legality of insider trading since 1980, when the Supreme Court focused on the issue of the SEC's regulatory authority in Chiarella v. United States.\(^\text{18}\) The securities statutes themselves do not forbid anyone to trade securities on the basis of material nonpublic information.\(^\text{19}\) The prohibition is contained in SEC rules, specifically rule 10b-5 and, if the information relates to a tender offer, rule 14e-3. These rules are written in broad terms that have generally been taken to encompass all trading by those who possess material nonpublic information about securities.\(^\text{20}\) Rule 10b-5 does not address insider trading explicitly,\(^\text{21}\) but it has always been taken as a sweeping rule


\(^{19}\) The Exchange Act does make it illegal to trade options while in possession of material nonpublic information if trading the underlying security would be illegal, but it does not say when trading the underlying security is illegal. 15 U.S.C. § 78t(d) (prohibiting the sale or purchase of options with respect to a security as to which the trader has material nonpublic information). Thus, even this limited statutory proscription of insider trading in derivatives is derivative of the sub-statutory law of insider trading. The Exchange Act also creates sanctions for insider trading that are tied to the violation of a rule. Id. §§ 78t(d), 78t-1, 78u-1 (all prohibiting the violation of rules promulgated under the statute).

\(^{20}\) See Dirks, 463 U.S. at 657 (1983) ("In effect, the SEC's theory of tippee liability in both cases appears rooted in the idea that the antifraud provisions require equal information among all traders."); Chiarella, 445 U.S. at 232. The Chiarella Court concluded that the court of appeals' decision thus rested solely upon its belief that the federal securities laws have created a system providing equal access to information necessary for reasoned and intelligent investment decisions . . . . The use by anyone of material information not generally available is fraudulent, this theory suggests, because such information gives certain buyers or sellers an unfair advantage over less informed buyers and sellers.

Id. (citations and internal quotation marks omitted). See also Bryan, 58 F.3d at 945 (discussing the broadest scope of rule 10b-5). But see O'Hagan, 1997 U.S. LEXIS 4033 at *66 (Scalia, J., dissenting in part) (arguing that the Court's construction of section 10(b) is not in accord with the principle of lenity applied to criminal statutes, "which cannot be mitigated here by the Rule, which is no less ambiguous than the statute"). The courts holding that the SEC exceeded its authority to regulate insider trading have not suggested that the trading at issue did not violate SEC rules. See O'Hagan, 92 F.3d at 615-57; Bryan, 58 F.3d 948-50.

\(^{21}\) See Donald C. Langevoort, Insider Trading and the Fiduciary Principle: A Post-Chiarella Restatement, 70 Cal. L. Rev. 1, 2-3 (1982) (stating that the development of insider trading law "has occurred even though neither the rule nor the statutory provision expressly prohibits insider trading. Rather, the law is almost entirely the product of judicial and administrative construction.").
that prescribes all manner of objectionable trading practices. Rule 14e-3 by its terms explicitly forbids trading by most people who possess nonpublic information about tender offers. While the SEC has aggressively tried to regulate insider trading, the difficult question since Chiarella has been whether it has the power to do so. Courts have looked to the language of sections 10(b) and 14(e) of the Exchange Act for the answer to that question.

The defendant in Chiarella was convicted of violating rule 10b-5 and section 10(b) of the Exchange Act because he bought the common stock of several companies after discovering, in the course of his employment as a financial printer, that his employer's customers planned to acquire that stock at premium prices. The Supreme Court reversed the conviction, holding that the government had to do more than simply demonstrate that the defendant bought securities while in possession of material nonpublic information. While its holding was narrow, the Court's explanation set the framework for all subsequent developments in the law of insider trading.

As it usually does in cases charging violations of rule 10b-5, the Court focused on the language of section 10(b) in Chiarella, explaining that the Exchange Act "cannot be read more broadly than its language and the statutory scheme permit." Section 10(b) makes it unlawful

\[22.\] Joseph A. Grundfest, Disimplying Private Rights of Action under the Federal Securities Laws: The Commission's Authority, 107 Harv. L. Rev. 963, 977 (1994) ("The expansive language of Rule 10b-5, and the Commission's sweeping interpretations, have caused the rule to become "as broad as almost any statute, a sort of long-arm provision in which the SEC forbids everything the statute gives it power to forbid." ") (quoting Thel, 42 Stan. L. Rev. at 463 (cited in note 12)). See Ernst & Ernst, 425 U.S. at 212 (observing that the language of rule 10b-5 can be read to proscribe any material omission and any conduct that has the effect of defrauding investors); Edward W. Kitch, A Federal Vision of Securities Law, 70 Va. L. Rev. 857, 861 (1984) (stating that "the SEC promulgated a regulation that spoke with the same generality as the statute" it was designed to implement); Donald C. Langevoort, Rule 10b-5 as an Adaptive Organism, 61 Fordham L. Rev. S7, S-11 to S-15 (1993) (outlining rule 10b-5's ability to mold the historical changes in the social perceptions of investing).

23. Recognizing the importance of statutory language, the courts which recently found that the SEC acted outside its regulatory authority devoted most of their opinions to manipulating the language of sections 10(b) and 14(e). See O'Hagan, 92 F.3d at 613 ("Neither the statutory language of section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), nor Supreme Court precedent interpreting it, will support the use of the 'misappropriation theory.' "); id. at 615-16 (dissecting the language of the statute); Bryan, 59 F.3d at 945 ("For at least two decades, however, the Supreme Court has repeatedly warned against expanding the concept of fraud in the securities context beyond what the words of the [Exchange] Act reasonably will bear."); id. at 944-50 (discussing the meaning of the language of § 10(b)).


25. Id. at 234 (quoting Touche Ross & Co., 442 U.S. at 578, quoting Sloan, 436 U.S. at 116) (internal quotation marks omitted). See also id. at 233 ("Formulation of such a broad duty... should not be undertaken absent some explicit evidence of congressional intent.").
to use any manipulative or deceptive device or contrivance in connection with the purchase or sale of a security in contravention of such rules as the SEC may prescribe as necessary or appropriate in the public interest or for the protection of investors. The complication in Chiarella, as in most insider trading cases, was that the defendant had not said anything to anyone, let alone lied.26 Given Chiarella’s silence, the problem was finding a deceptive device.27 The Court held that silence is not deceptive (the Court used the word “fraudulent”) within the meaning of section 10(b) unless the silent party has a duty to speak, and that mere possession of nonpublic information does not give rise to such a duty.28 This holding dictated reversal, since the trial court had not required the government to prove that the defen-

The Supreme Court summarized its history with rule 10b-5 recently, and in so doing accurately emphasized the critical importance it has ascribed to the language of section 10(b) in its rule 10b-5 cases:

In our cases addressing § 10(b) and Rule 10b-5, we have confronted two main issues. First, we have determined the scope of conduct prohibited by § 10(b). See, e. g., Dirks v. SEC, 463 U.S. 646 (1983); Aaron v. SEC, 446 U.S. 680 (1980); Chiarella v. United States, 445 U.S. 222 (1980); Santa Fe Industries, Inc. v. Green, 430 U.S. 462 (1977); Ernst & Ernst v. Hochfelder, 425 U.S. 185 (1976). Second, in cases where the defendant has committed a violation of § 10(b), we have decided questions about the elements of the 10b-5 private liability scheme: for example, whether there is a right to contribution, what the statute of limitations is, whether there is a reliance requirement, and whether there is an in pari delicto defense.

With respect, however, to the first issue, the scope of conduct prohibited by § 10(b), the text of the statute controls our decision . . . our cases considering the scope of conduct prohibited by § 10(b) in private suits have emphasized adherence to the statutory language, “the starting point in every case involving construction of a statute.” Ernst & Ernst, 425 U.S. at 197 (quoting Blue Chip Stamps, 421 U.S. at 756 (Powell, J., concurring)). See Chiarella, 445 U.S. at 226; Santa Fe Industries, 435 U.S. at 472. We have refused to allow 10b-5 challenges to conduct not prohibited by the text of the statute. Central Bank, 511 U.S. at 172-73. See also id. at 175 (“Our consideration of statutory duties, especially in cases interpreting § 10(b), establishes that the statutory text controls the definition of conduct covered by § 10(b).”); id. at 177 (“It is inconsistent with settled methodology in § 10(b) cases to extend liability beyond the scope of conduct prohibited by the statutory text.”); Aaron v. SEC, 446 U.S. 680, 689-90 (1980) (emphasizing the primacy of “the plain meaning of the language of § 10(b)”); Ernst & Ernst, 425 U.S. at 213-14 (“The rulemaking power granted to an administrative agency charged with the administration of a federal statute is not the power to make law. Rather, it is the power to adopt regulations to carry into effect the will of Congress as expressed by the statute.”) (internal quotation marks omitted).

26. Chiarella, 445 U.S. at 226 n.5. See Aaron, 446 U.S. at 689-95 (SEC must prove scienter as an element of its civil enforcement action); Ernst & Ernst, 425 U.S. at 212-15 (plaintiff must prove scienter in private action for violation of rule 10b-5).

27. Chiarella, 445 U.S. at 226 (“§ 10(b) does not state whether silence may constitute a manipulative or deceptive device.”). The Supreme Court has largely read “manipulative” out of section 10(b), at least in the context of insider trading regulation. Ernst & Ernst, 425 U.S. at 198 (stating that the word manipulative is “virtually a term of art when used in connection with securities markets”). See Aaron, 446 U.S. at 690 (equating “manipulative” with “device” or “contrivance”); O’Hagan, 92 F.3d at 615 n.4 (focusing on the “deception,” not the “manipulative,” component of § 10(b)); Bryan, 58 F.3d at 945-46 (same).

dant was under any duty to disclose information before trading. Instead, the trial court had permitted the jury to convict upon a mere finding that the defendant had traded while in possession of material nonpublic information.29

Although the Court held that section 10(b) does not forbid all trading by those in possession of material nonpublic information, it did not say that such trading is always legal. On the contrary, the Court indicated that corporate insiders have a duty to disclose material nonpublic corporate information before buying corporate stock, because of "the relationship of trust and confidence between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation."30 Since silence in the face of a duty of disclosure is deceptive within the meaning of section 10(b), corporate insiders who buy common stock from public stockholders without disclosing material nonpublic corporate information are guilty of deception and thus violate rule 10b-5 and section 10(b).31

This theory of insider trading liability captures senior corporate employees who buy their employer's common stock after obtaining material nonpublic information during the course of their employment. However, those who do not work for the issuer of trade securities fall outside of the scope of the restriction inasmuch as such people have no obvious "relationship of trust and confidence" with the issuer's shareholders.32 The disclosure duty recognized in Chiarella—the fiduciary duty of candor that corporate insiders owe to owners of corporate equity securities—may not be implicated when someone trades on the basis of material nonpublic information that is not obtained directly or indirectly from the issuer of the traded securities, even if that information is obtained improperly. If this duty of candor is not implicated, then such "outsider" trading is illegal only if it is deceptive (or fraudulent) in some other sense.

B. The Misappropriation Doctrine and Rule 14e-3

Chiarella appeared to be a substantial setback for those who objected to people trading while in possession of material nonpublic information. Very quickly, however, the SEC developed two related

29. Id. at 235.
30. Id. at 228.
31. Id. at 230.
32. See Langevoort, 70 Cal. L. Rev. at 44-52 (cited in note 21) (discussing misappropriation theories).
tools to recover the initiative: the misappropriation doctrine under rule 10b-5 and rule 14e-3. The misappropriation doctrine builds on the Supreme Court's approach to insider trading by tying insider trading regulation to the trader's participation in the breach of an independent fiduciary duty, the duty not to steal; whereas, in Chiarella, the Court focused on the fiduciary's duty to disclose. Rule 14e-3, in contrast, amounts to adoption of a principle of equal access to information about tender offers, which is justified (if justified at all) by being grounded in section 14(e) of the Exchange Act instead of the arguably narrower grant of rule-making authority in section 10(b).

Even before the Supreme Court decided Chiarella, the SEC had proposed rule 14e-3, which would have established for tender offers something close to the parity-of-information regime that the Court rejected. In 1980, a few months after the Court decided Chiarella, the SEC went ahead and adopted its rule. Rule 14e-3 provides that once someone has taken a substantial step to commence a tender offer for a security, no one else in possession of material nonpublic information relating to such offer may trade that security (or any security derived from it) if she has reason to know the information came from the offeror or the issuer of the security or from affiliates or agents of either.33

Although the Commission adopted rule 14e-3 in the shadow of Chiarella, it did not attempt to justify the rule as a regulation of deception, at least not deception in the narrow sense in which Chiarella defined it. The Commission grounded rule 14e-3 in sections 14(e) and 23(a) of the Exchange Act,34 rather than on section 10(b). The Exchange Act can be read to give the Commission greater rulemaking power under section 14(e) than under section 10(b).35 The Commission certainly claimed as much, insisting that Chiarella did not "suggest any limitation on the commission's authority under Section 14(e) to adopt a rule regulating trading while in possession of material, nonpublic information relating to a tender offer."36

Rule 14e-3 was held to be within the SEC's authority shortly after it was adopted,37 and, for a while, every court that considered the

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35. The Supreme Court seemed to recognize this possibility in Chiarella. See Chiarella, 445 U.S. at 234 (discussing SEC's proposal of rule 14e-3).


question agreed that the SEC had acted within its power in adopting the rule. The Supreme Court has now held that, at least insofar as it serves to prevent trading on the basis of misappropriated information after a tender offer has commenced, “Rule 14e-3 is a proper exercise of the Commission’s prophylactic power under § 14(e).” Nonetheless, the validity of rule 14e-3 was clearly questionable when the SEC adopted it and when Congress acted in 1988.

Section 14(e) of the Exchange Act makes it unlawful for any person to engage in any fraudulent, deceptive, or manipulative acts or practices in connection with any tender offer, and further provides that the SEC “shall... by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative.” If Chiarella did not limit the SEC's power under section 14(e), it is either because the word “deceptive” has a broader meaning in section 14(e) than in section 10(b), or because the SEC has greater rulemaking power under section 14(e) than it has under section 10(b). However, in a 1985 decision narrowly construing section 14(e), Burlington Northern, Inc. v. Schreiber, the Supreme Court emphasized the similarities between section 14(e) and section 10(b), and its opinion can be read to suggest that section 14(e)'s language should be construed as narrowly as section 10(b)'s. If it were, rule 14e-3 would seem an invalid administrative attempt to make law. In the end, ample proof that the rule's foundation was at least suspect is provided not only by Schreiber and the criticism of academic commentators, but also by the Eighth Circuit's decision that it was invalid in O'Hagan and Justice Thomas's dissent from that decision's reversal.

39. O'Hagan, 1997 U.S. LEXIS 4033 at *60. The Court did not address Mr. O'Hagan's argument that rule 14e-3 is invalid because it prohibits trading in advance of tender offers. See id. at *61.
42. Id. at 6-10.
43. See John F. Olson, John H. Sturc, and Gerald T. Lihs, Recent Insider Trading Developments: The Search for Clarity, 86 Nw. U. L. Rev. 715, 735-37 (1991) (discussing recent case law which rejects the Commission's use of Rule 14e-3); Brent G. Stahl, Note, Rule 14e-3: Invalid in the Criminal Context, 16 Am. J. Crim. L. 361, 367-80 (1979) (arguing that the disclose or abstain provisions of Rule 14e-3 should be held invalid under the Rule of Lenity).
44. O'Hagan, 92 F.3d at 627. See Part II.C (Discussing the Eighth Circuit's decision in O'Hagan).
The other attempt to avoid the restrictions of Chiarella was the misappropriation doctrine. Until the Supreme Court decided O'Hagan, the only form of trading on material nonpublic information that the Court had said the SEC could regulate under section 10(b) was trading by corporate insiders and, in some cases, their tippees.45 Nonetheless, as the SEC noted when it adopted rule 14e-3,46 the Court never expressly foreclosed the possibility that section 10(b) and rule 10b-5 may forbid others to trade on the basis of material nonpublic information. In particular, the Court in Chiarella did not address the government's theory that section 10(b) and rule 10b-5 require persons who possess misappropriated nonpublic information to disclose that information or abstain from trading.47 Since the trial judge did not submit this theory to the jury, the Court declined to “speculate” on whether it would support a conviction for violation of section 10(b).48

Shortly after Chiarella was decided and about the same time the SEC adopted rule 14e-3, the Second Circuit concluded that section 10(b) and rule 10b-5 make it unlawful for a person to trade in securities in breach of fiduciary duty by secretly converting for personal use information that has been entrusted to him.49 Thereafter, several other courts followed and held that rule 10b-5 makes it unlawful to trade on the basis of misappropriated material nonpublic information in violation of a duty owed to the source of the information, and that the SEC has authority to forbid such trading even if the trader owes no duty of disclosure to the other party to the trade.50

45. Dirks, 463 U.S. at 653-60.
46. See Release No. 17,120 at 83,456 (cited in note 33) (“[T]he Chiarella Court did not resolve whether trading while in possession of material, nonpublic market information misappropriated or obtained or used by unlawful means violates Rule 10b-5. The Commission continues to believe that such conduct undermines the integrity of, and investor confidence in, the securities markets, and that persons who unlawfully obtain or misappropriate material, nonpublic information violate rule 10b-5 when they trade on such information.”).
47. Chiarella, 445 U.S. at 236-37. The concurring and dissenting opinions seemed quite sympathetic to the misappropriation doctrine. See id. at 238 (Stevens, J., concurring) (“[A] legitimate argument could be made that [Chiarella's] actions constituted a fraud or a deceit.”); id. at 239 (Brennan, J., concurring in the judgment) (stating that “a person violates § 10(b) whenever he improperly obtains or converts to his own benefit nonpublic information”); id. at 240-45 (Burger, J., dissenting) (advocating a broad application of the misappropriation theory); id. at 245 (Blackmun and Marshall, JJ., dissenting) (agreeing with Justice Burger's view that § 10(b) encompasses the misappropriation theory).
48. See, for example, United States v. Newman, 664 F.2d 12, 16 (2d Cir. 1981).
50. See, for example, United States v. Cherif, 933 F.2d 403 (7th Cir. 1991); SEC v. Clark, 915 F.2d 439 (9th Cir. 1990); United States v. Libera, 989 F.2d 596 (2d Cir. 1993); SEC v. Lentfest, 1996 U.S. Dist. LEXIS 18861 (E.D. Pa.); SEC v. Materia, 745 F.2d 197 (2d Cir. 1984); SEC v. Willis, 787 F. Supp. 58 (S.D.N.Y. 1992); SEC v. Singer, 786 F. Supp. 1158 (S.D.N.Y. 1992). But see Chestman, 947 F.2d at 551, 570-71 (endorsing doctrine but finding no duty in family relation-
The success of the misappropriation doctrine paralleled that of rule 14e-3. For a long time, every court faced with the question concluded that trading on the basis of misappropriated material nonpublic information violates section 10(b) and rule 10b-5, and further that the SEC had authority to regulate such trading. However, this judicial acceptance does not mean courts were correct in these holdings, or even that the parameters of the doctrine were clear. On the contrary, the validity of the misappropriation doctrine was arguably even more tenuous than that of rule 14e-3. As with the rule, some commentators have criticized the doctrine, and, like the rule, some courts essentially held it to be an invalid SEC attempt to make law.

The Supreme Court's 1987 opinion in United States v. Carpenter made the weakness of the misappropriation doctrine's foundation vividly clear. Carpenter involved a Wall Street Journal columnist and several stock brokers who profitably traded securities in advance of their mention in the Journal's "Heard on the Street" column, apparently in contravention of Journal policy. The Second Circuit affirmed criminal convictions for violations of section 10(b), rule 10b-5, and the mail and wire fraud statutes, and in doing so firmly endorsed a broad scope for the misappropriation doctrine. The Supreme Court unanimously affirmed the convictions on the mail and

ship); Rothberg v. Rosenbloom, 771 F.2d 818, 822 (3d Cir. 1985) (arguably endorsing misappropriation doctrine).

51. See Chestman, 947 F.2d at 564-71, 573-81 (en banc court splitting over whether information was misappropriated within meaning of the doctrine); Wang and Steinberg, Insider Trading at 381-389 (cited in note 1) (discussing open questions for misappropriation doctrine); Bainbridge, 52 Wash. & Lee L. Rev. at 1243-45 (cited in note 12) (same); John R. Beeson, Comment, Rounding the Peg to Fit the Hole: A Proposed Regulatory Reform of the Misappropriation Theory, 144 U. Pa. L. Rev. 1077, 1125-40 (1996) (same).

52. See notes 38 and 41 and accompanying text (comparing the authority given to the SEC under §§ 14(e) and 10(b)).


54. O'Hagan, 92 F.3d at 622; Bryan, 89 F.3d at 953-55. See also Part II.C (discussing O'Hagan and Bryan).


wire fraud counts and discussed them extensively. However, the Court was evenly divided on the question of whether trading on the basis of misappropriated information violates section 10(b) and rule 10b-5. The Court explained simply: “The Court is evenly divided with respect to the convictions under the securities laws and for that reason affirms the judgment below on those counts.”

In sum, by 1988—an important year in this story—the narrow insider-trading rule that survived Chiarella had been supplemented by the SEC’s rule 14e-3 and the misappropriation doctrine under rule 10b-5. The basic structure of the misappropriation doctrine was settled, at least in broad outline, and courts had shown themselves willing to decide difficult questions of its scope without further guidance from Congress. The scope of rule 14e-3 was quite clear, because the rule itself spoke in direct terms. Yet even if the scope of the prohibitions were largely clear in 1988, their effects were not—both rule 14e-3 and the misappropriation doctrine rested on uncertain statutory ground.

Each was based on a construction of statutory language that stretched the limits of Chiarella, and although no court had rejected the rule or the doctrine, critics had questioned the validity of both while most courts had not had occasion to consider either. More importantly, Carpenter suggested that the Supreme Court was uncomfortable with the misappropriation doctrine; and if that doctrine was invalid, then, in light of Schreiber, rule 14e-3 might be invalid too.

C. The Attack on the Misappropriation Doctrine and Rule 14e-3

Rule 14e-3 and the misappropriation doctrine both suffered under judicial scrutiny after Carpenter. In 1991, the Second Circuit, which had been the court most sympathetic to the misappropriation doctrine, signaled that the doctrine could not be extended to guarantee equal access to material information. In its en banc decision in United States v. Chestman, the court held that a member of a family that controlled a public company did not breach any duty of confidentiality when he leaked information about an impending tender offer to a stockbroker. Accordingly, the court held that the broker did not violate rule 10b-5 when he traded on the basis of the tipped information.

tion, even under the misappropriation doctrine.\textsuperscript{61} The court, however, did affirm the broker’s conviction for violating rule 14e-3,\textsuperscript{62} albeit over a dissent arguing that the Commission had exceeded its authority.\textsuperscript{63}

After Chestman, the misappropriation doctrine and rule 14e-3 were attacked more successfully. In 1995, in United States v. Bryan,\textsuperscript{64} the Fourth Circuit rejected the misappropriation doctrine, reasoning that even if the breach of trust that underlies a finding of misappropriation is deceptive,\textsuperscript{65} section 10(b) “reaches only deception of persons with some connection to, or some interest or stake in, an actual or proposed purchase or sale of securities.”\textsuperscript{66} The court refused to find that a person who misappropriates information from one person and then trades with another person violates section 10(b).\textsuperscript{67} According to the court, “neither the language of section 10(b), Rule 10b-5, the Supreme Court authority interpreting these provisions, nor the purposes of these securities fraud prohibitions, will support convictions resting on the particular theory of misappropriation adopted by our sister circuits.”\textsuperscript{68}

Last year, in United States v. O’Hagan,\textsuperscript{69} the Eighth Circuit followed Bryan and held “that § 10(b) liability cannot be based on the misappropriation doctrine.”\textsuperscript{70} The court went further, however, and also held that “the SEC exceeded its rulemaking authority by enacting

\textsuperscript{61} Id. at 570-71. But see United States v. Reed, 601 F. Supp. 685, 720 (S.D.N.Y. 1985) (holding a jury could find that son violated rule 10b-5 by trading on material nonpublic information obtained from father), rev’d on other grounds, 773 F.2d 477 (2d Cir. 1985). The Second Circuit declined to overturn Reed in Chestman, 947 F.2d at 568. Judge Winter dissented from Chestman’s restriction on the scope of the misappropriation theory, but not on the ground that the broker violated the rules established by Chiarella and Dirks—or even any coherent theory of what is illegal—but instead on the theory that “the law is far enough down this road . . . that a court of appeals has no option but to continue the route.” Id. at 578.

\textsuperscript{62} Id. at 555-63.

\textsuperscript{63} Id. at 583-88 (Mahoney, J., concurring in part and dissenting in part).


\textsuperscript{65} See Bryan, 58 F.3d at 942 (“Even if the misappropriation theory required deception, or deception were otherwise present, the theory still does not require deception violative of fair representation or disclosure owed to a market participant . . . .”).

\textsuperscript{66} Id. at 950.

\textsuperscript{67} Id. But see Part III.B (questioning this holding).

\textsuperscript{68} Bryan, 58 F.3d at 944.

\textsuperscript{69} 92 F.3d 612.

\textsuperscript{70} Id. at 617. See id. at 613 (“[N]either the statutory language of section 10(b) nor the Supreme Court precedent interpreting it will support the use of the misappropriation theory.”); id. at 620 (“We find the analysis from Bryan persuasive and have borrowed heavily from it in arriving at our conclusion. Therefore, we adopt that court’s analysis in its entirety as our own.”).
Rule 14e-3(a) without including the requirement of a breach of a fiduciary duty. The court rejected rule 14e-3 for essentially the same reason it rejected the misappropriation doctrine under section 10(b) and rule 10b-5. As the court saw it, "although perhaps § 14(e) is the product of clearer legislative draftsmanship [than is section 10(b)], the authority granted to the SEC under both provisions is fundamentally the same." It followed that since the Commission could not forbid trading on the basis of misappropriated information under section 10(b), it could not forbid even more under section 14(e).

The Supreme Court reversed the Eighth Circuit's decision in O'Hagan, and in doing so it rejected the analysis of Bryan as well. The Court held that the language of section 10(b) encompasses trading on the basis of misappropriated information, and that the SEC had the power under section 14(e) to adopt rule 14e-3. The Court's interpretation of sections 10(b) and 14(e) is reasonable, but it is not the only reasonable interpretation of the statute. Two circuit courts of appeal and dissenting justices in O'Hagan read the statute otherwise. Indeed, whoever was right about what sections 10(b) and 14(e) mean, the reason the Court had to decide O'Hagan was that its own earlier insider trading cases had raised doubts about the SEC's authority to regulate trading like that of Mr. O'Hagan. The 1988 Act, however, directly addresses that authority, and it did so precisely to resolve the doubts that the Court had created.

III. THE 1988 ACT AND THE SEC'S POWER TO REGULATE INSIDER TRADING

The sketch of the rules governing insider trading set out above focused on the law as it has developed in the courts. This focus on judicial developments echoes the conventional wisdom that the courts have decided what kinds of trading are unlawful, under prodding from the SEC, with Congress stepping in only to increase the penalties from time to time. Thus the Eighth Circuit in O'Hagan insisted that Congress has done nothing since enacting section 10(b) and 14(e) that is relevant to the validity of the misappropriation doctrine and rule

71. Id. at 634. See id. at 614, 627 (finding that the SEC had exceeded its authority in promulgating Rule 14e-3(a) without requiring a breach of fiduciary duty obligation).
72. Id. at 626.
73. 1997 U.S. LEXIS 4033.
74. See notes 15-23 and accompanying text (discussing the evolution of the Court's treatment of insider trading).
Nevertheless, several recent federal statutes deal with insider trading, and the 1988 Act explicitly addressed the validity of the SEC's rules against insider trading.

A. The 1988 Act and the Law of Insider Trading

The better-known provisions of the 1988 Act increased sanctions against illegal insider trading. They amended the Exchange Act to increase the criminal penalties for violations of the Exchange Act; to authorize the SEC to seek civil penalties against those who violate the Exchange Act or its regulations by trading securities while in possession of material nonpublic information; to require brokers and dealers to establish policies and procedures designed to prevent the illegal misuse of material nonpublic information; and to establish an explicit private right of action for contemporaneous traders against those who violate the Exchange Act by trading securities while in possession of material nonpublic information.

Congress did not define insider trading in the 1988 Act, despite substantial pressure to do so. Instead, the 1988 Act's sanctions attach to insider trading that is forbidden by other parts of the securities laws. They are available when someone violates any provision of the Exchange Act or its rules "by purchasing or selling a security while in possession of material, nonpublic information." The House Energy and Commerce Committee offered two justifications for its

75. 92 F.3d at 626 n.17. But see Bainbridge, 52 Wash & Lee L. Rev. at 1204-05 (cited in note 12) (criticizing Bryan for failing to consider reenactment doctrine).


82. 1988 Act § 21A (a) (I).
decision not to set out a precise prohibition in the statute. First, it was satisfied that court decisions had established relatively clear legal guidelines already. The Committee felt that a statutory definition inadvertently might have narrowed the law and provided a sort of roadmap to fraud that would have enabled traders to evade the law. Second, it felt that the enactment of the sanctions provided in the statute should not be delayed by debate over a definition of insider trading.83

Although the sponsors of the 1988 Act did not want to enact a complete statutory statement of when insider trading is illegal, they apparently did want to indicate that the trading that the courts had held to be illegal should remain illegal.84 Toward that end, section 2 of the statute provides that

The Congress finds that—
(1) the rules and regulations of the Securities and Exchange Commission under the Securities Exchange Act of 1934 governing trading while in possession of material, non-public information are, as required by such Act, necessary and appropriate in the public interest and for the protection of investors;
(2) the Commission has, within the limits of accepted administrative and judicial construction of such rules and regulations, enforced such rules and regulations vigorously, effectively, and fairly; and
(3) nonetheless, additional methods are appropriate to deter and prosecute violations of such rules and regulations.85

As discussed below, the rules to which these findings refer are rule 10b-5 and rule 14e-3. If these rules are, as the findings state, necessary and appropriate in the public interest and for the protection of investors, then rule 14e-3 is a valid and enforceable rule, and trading on the basis of misappropriated nonpublic information is a violation of rule 10b-5 and section 10(b). Rule 14e-3 and the misappropriation doctrine have been controversial precisely because of questions about whether the SEC has statutory authority to regulate what it purports to regulate. The Exchange Act authorizes the SEC to adopt


84. The legislative history indicates that the statute was intended to show support for the SEC’s enforcement initiatives. See House Report at 35 (cited in note 81) (“These findings are intended as an expression of congressional support for [the SEC’s] regulation.”). See also Kaswell, 46 Bus. Law. at 157-58 (cited in note 12) (discussing the findings as an explicit endorsement of the SEC’s enforcement efforts).

necessary or appropriate rules, and if either rule 14e-3 or the misappropriation doctrine under rule 10b-5 exceeded the Commission's statutory authority, it would be because they are not necessary or appropriate. Conversely, if the rules are necessary and appropriate, the misappropriation doctrine and rule 14e-3 are enforceable under the provisions of the Exchange Act providing for enforcement of SEC rules.

86. 15 U.S.C. § 78w(a)(1) (1994) (granting the SEC authority to adopt "such rules and regulations as may be necessary or appropriate to implement the provisions of" the Exchange Act). See also id. § 78j(b) (referring to "such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors").

87. One might argue that even if trading on the basis of misappropriated information violates rule 10b-5, and even if the rule is necessary and appropriate in the public interest, such trading is still not manipulative or deceptive, and hence it does not violate section 10(b). This reading of the statute takes section 10(b) not as a delegation of rule-making authority but simply as a device to make the violation of some SEC rules criminal, with rulemaking authority delegated (only) by section 23(a) of the Exchange Act. See 15 U.S.C. § 78ff(a) (containing criminal sanctions for violations of rules, the violation of which is made unlawful by the statute). The Supreme Court might have had this interpretation of section 10(b) in mind in O'Hagan when it said that "liability under Rule 10b-5, our precedent indicates, does not extend beyond conduct encompassed by § 10(b)'s prohibition," 1997 U.S. LEXIS 4033 at *19, and noted that Mr. O'Hagan had not challenged rule 10b-5's promulgation. Id. at *30. However, the Court also cited Ernst & Ernst for the proposition that the scope of rule 10b-5 cannot exceed the power granted to the SEC by section 10(b), id. at *19, and it did not suggest that it was adopting a new approach to rule 10b-5 and section 10(b). In any event, while the theory that section 10(b) is only a sanctioning provision and not a grant of rule-making authority is clever, it is probably inconsistent with the history and structure of the Exchange Act and it has been implicitly rejected by the Supreme Court, which has always treated section 10(b) as a grant of rule-making authority. Moreover, even if section 10(b) were taken to be merely a sanctioning provision (triggering criminal penalties under section 32(a)), violations of rule 10b-5 would still be punishable under other provisions of the Exchange Act, which attach to violations of any SEC rule, not just those of the violation of which is made unlawful by other provisions of the Act. Thei, 42 Stan. L. Rev. at 388 n.20, 390 n.24 (cited in note 12) ("It is probably correct to say that § 10(b) was intended to authorize the SEC to regulate conduct. The Supreme Court has always interpreted it that way."). See, for example, 15 U.S.C. §§ 78t(d), 78u(d), 78u-1, 78u-2 (1994) (all prescribing penalties or liability for "any provision of this chapter"). In any event, in 1988, section 10(b) was universally regarded as granting the SEC rule-making authority and the structure of the findings indicate that Congress accepted this view. Accordingly, to the extent that the 1988 findings declare that the SEC has authority to enforce the misappropriation doctrine under section 10(b), they should also be taken as a declaration that anyone who violates rule 10b-5 by trading on misappropriated nonpublic information has also violated section 10(b). See House Report at 10 (cited in note 81) ("In the view of the Committee, however, this type of security fraud [i.e., fraud prohibited by the misappropriation doctrine] should be encompassed within Section 10(b) and Rule 10b-5.").

88. See, for example, Exchange Act §§ 20(d)(1) (SEC-initiated injunctive actions for violations of rules), 21A (civil penalties for insider trading), 32(a) (criminal penalties for violations of rules the violation of which is made unlawful by the Act), 15 U.S.C. §§ 78u(d)(1), 78u-1, 78ff(a) (1994).
B. The Scope of the 1988 Findings

Before addressing the question of what force the 1988 findings may have, it is necessary to identify the rules to which they refer in order to understand what they were supposed to accomplish (or even mean). As a matter of fact, the rules to which the findings refer are rules 10b-5 and 14e-3 and no one with knowledge of what was happening in 1988 would suggest otherwise. In addition, the history of the legislation clearly indicates that Congress intended to validate rule 14e-3 and to codify the Second Circuit's approval of the misappropriation doctrine and extend it nationally.89 Simply put, in 1988 the words “the rules and regulations of the Securities and Exchange Commission under the Securities Exchange Act of 1934 governing trading while in possession of material, non-public information” meant rules 10b-5 and 14e-3.

As a formal matter, the findings presumably refer to some actual rules when they refer to rules, and analysis of the 1988 Act—even independent of its legislative history and contemporary understanding—indicates that the rules referred to in the findings are rules 10b-5 and 14e-3. Rule 14e-3 is the simpler case. The rule makes it unlawful for a person to trade securities while “in possession of

89. According to the House Energy and Commerce Committee, the only committee that reported on the 1988 Act,

Although there is no statutory “definition” of insider trading, this activity is prescribed by provisions of the securities laws, including Section 17(a) of the Securities Act, Sections 10(b) and 14(e) of the Securities Exchange Act of 1934, and Section 206 of the Investment Advisers Act, and the case law that has developed over time interpreting those provisions.

Within the court-developed parameters for insider trading, courts that have addressed the issue have also broadened the doctrine of insider trading to include trading and tipping by persons who misappropriate material nonpublic information from sources other than market participants. That was the theory underlying the case of United States v. Carpenter, 791 F.2d 1024 (2d Cir. 1986), aff'd on securities law counts by an equally divided court, 108 S. Ct. 316 (1987).

The Supreme Court addressed the “misappropriation” theory of insider trading last November, in the appeal of the Carpenter case, and reached no definitive decision. . . . The Court divided on a 4-4 vote on the question of whether Winans’ “misappropriation” of information rightfully belonging to his employer constituted insider trading, even absent any direct fiduciary duty [owed] from Winans to the issuers or purchasers and sellers of the securities. The Court's opinion contained no discussion of the issue. Thus the misappropriation doctrine clearly remains valid in the Second Circuit, the lower Court in the Winans case, but is unresolved nationally. In the view of the Committee, however, this type of security fraud should be encompassed within Section 10(b) and Rule 10b-5.

House Report at 5, 10 (cited in note 81). See also id. at 35 (“These findings are intended as an expression of congressional support for these regulations.”); 134 Cong. Rec. E3078 (Sept. 23, 1988) (statement of Rep. Markey, principal author of the 1988 Act) (“One area in which there is strong congressional consensus is the validity of the ‘misappropriation’ theory of insider trading.”).
material information . . . he knows or has reason to know is non-public," so it is quite plainly a rule "governing trading while in possession of material non-public information."

The findings' reference to the misappropriation doctrine under rule 10b-5 is a little more complicated. Unlike rule 14e-3, rule 10b-5 does not by its terms speak to trading on the basis of material nonpublic information. Instead, it broadly proscribes all schemes to defraud as well as any act that would operate as a fraud. Nevertheless, rule 10b-5 is a rule that governs trading while in possession of material nonpublic information. The Supreme Court itself has said repeatedly that rule 10b-5 and section 10(b) govern some trading while in possession of material nonpublic information (and it said so before 1988). 90 Indeed, rule 10b-5 is and has been the rule most frequently used to govern trading by those in possession of material nonpublic information, 91 because the rule does govern trading while in possession of material nonpublic information. It simply governs other conduct touching the securities markets as well. 92

The conclusion that the findings refer to the misappropriation doctrine is reinforced by the second finding, that "the Commission has, within the limits of accepted administrative and judicial construction of such rules and regulations, enforced such rules and regulations vigorously, effectively, and fairly." The misappropriation doctrine was well known in 1988, and everyone in Congress involved with the 1988 Act was familiar with it. The misappropriation doctrine had figured prominently in the contemporaneous debate over whether to enact a statutory definition of insider trading. 93 As the legislative history of the 1988 Act reflects, those responsible for the 1988 Act were willing to dispense with an explicit definition precisely because they knew that every court faced with the issue had held that the SEC had authority under section 10(b) to prohibit trading on the basis of misappropriated information. 94 As the legislative history of the findings

90. See Chiarella, 445 U.S. at 231-35 (suggesting that fraud can occur under § 10(b) if the person in possession of nonpublic information owes a fiduciary duty to investors); Dirks, 463 U.S. at 654-65 (same); Carpenter, 484 U.S. at 24 (affirming a rule 10b-5 conviction for trading on misappropriated information).

91. When the 1988 Act was enacted, it was "well known that the basic prohibitions against insider trading arise from judicial interpretations of the general anti-fraud provisions of section 10(b) of the Exchange Act and rule 10b-5." Kaswell, 45 Bus. Law. at 152 (cited in note 12). See also House Report at 7-11 (cited in note 81) (discussing rule 10b-5 extensively).

92. See Part II.A (discussing the broad scope of the insider trader regulations).

93. See note 81 and accompanying text (discussing Congress's concern and focus on whether to define insider trading).

94. See note 83 and accompanying text (explaining why Congress did not define insider trading in the 1988 Act).
reflects, in 1988 the “accepted administrative and judicial construction” was that the misappropriation doctrine and rule 14e-3 were rules that governed trading while in possession of material nonpublic information. While the validity of the doctrine and rule 14e-3 might have been open to question before Congress acted, every court that had spoken on this issue had construed section 10(b) and rule 10b-5 to forbid trading on the basis of misappropriated material nonpublic information and construed section 14(e) and rule 14e-3 to forbid trading on the basis of material nonpublic information about a tender offer.

If the findings’ reference to rule 10b-5 is at all unclear, it is because the findings might be read more broadly to validate the whole of rule 10b-5, not just its proscription of insider trading. By their terms and structure, the findings indicate that rule 10b-5 as a whole is necessary and appropriate, and not just those aspects of the rule that govern trading while in possession of material nonpublic information. Rule 10b-5 is a rule governing trading while in possession of material nonpublic information, and the findings say that such rules are within the statutory power granted to the SEC.

If the reference to rule 10b-5 in the 1988 findings is a reference to the whole rule, then the findings validate the whole rule, including its entire prohibition of insider trading. A general validation of rule 10b-5 would preempt any argument that the rule reaches conduct that the SEC is not authorized to regulate, even conduct that has nothing to do with insider trading. While this broad reading may be dictated by the Supreme Court’s securities-statute literalism, it is surely not what was intended by those responsible for the 1988 Act. The

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95. House Report at 8-10 (cited in note 81).
96. In his dissent in O’Hagan, Justice Thomas suggested that a broad delegation of rule-making power to the SEC might be problematic. See 1997 U.S. LEXIS 4033 at *86 (“Putting aside the dubious validity of an open-ended delegation to an independent agency to go forth and create regulations criminalizing ‘fraud’ . . . .”). See also id. at *93 n.10 (“A law that simply stated ‘it shall be unlawful to do ‘X’, however ‘X’ shall be defined by an independent agency,’ would seem to offer no ‘intelligible principle’ to guide the agency’s discretion and would thus raise very serious delegation concerns, even under our current jurisprudence.”).

Given the breadth of the language of rule 10b-5, the consequences of a broad reading of the findings might be quite interesting. By its terms, rule 10b-5 forbids negligent misrepresentations. See Ernst & Ernst, 425 U.S. at 212-14 (“When a statute speaks so specifically in terms of manipulation and deception . . . we are quite unwilling to extend the scope of the statute to negligent conduct.”); Aaron, 446 U.S. at 695-700 (construing language in section 17(a) of the Securities Act that is substantially identical to rule 10b-5 to encompass negligent misrepresentations). If the findings make rule 10b-5 binding as a whole, they effectively might reverse Hochfelder and Aaron, each of which held that scienter is an element of a section 10(b) violation. The second finding, which can be read to express approval of court-set limits on the SEC, might be read to save those decisions.
legislative history of the 1988 Act and the operation of its other provisions both focus primarily on insider trading.97

Perhaps a narrow construction of the findings (as encompassing rules only to the extent that they govern insider trading) can be based on the fact that the findings refer not to rules governing fraud generally, but instead to rules governing insider trading. More technically, the second finding's reference to the "limits of accepted administrative and judicial construction of such rules,"98 which quite apparently refers to the cases on the misappropriation doctrine, can work to restrict the findings' scope to rule 14e-3 and the insider-trading aspects of rule 10b-5.

No court has construed the 1988 findings, but courts have construed similar language in other provisions of the 1988 Act to refer to rule 14e-3 and the insider-trading aspect of rule 10b-5 (and only to that aspect of the rule). Their uniform construction of the 1988 Act reinforces the conclusion that the rules referred to in the findings are rule 14e-3 and rule 10b-5, and that the findings refer to rule 10b-5 only to the extent that it governs insider trading.

As noted above, among the sanctions that the 1988 Act added to the Exchange Act was a private right of action for contemporaneous traders against anyone who violates SEC rules by purchasing or selling a security while in possession of material nonpublic information.99 This private right of action includes its own five-year limitations period.100 When the limitations period for rule 10b-5 actions was in controversy, some plaintiffs argued that this five-year period should govern all private rule 10b-5 litigation. Courts consistently rejected this argument, holding that the five-year period governs only actions against those who trade while in possession of material nonpublic information. In doing so, the courts repeatedly emphasized that the rules that forbid people to trade while in possession of material nonpublic information, which are the rules that are referred to in the findings as well as the rules that trigger the private right of action for contemporaneous traders, are rules 10b-5 and 14e-3.101


98. 1988 Act § 2(2).

99. 15 U.S.C. § 78t-1(a) (1994); see id. § 78t(d) (private right of action for contemporaneous option traders).

100. Id. § 78t-1(b)(4).

Rule 10b-5 governs trading while in possession of material non-public information in two situations: traditional insider trading of the sort the Supreme Court said was unlawful in *Chiarella*, and trading on the basis of misappropriated information. The findings should be read to refer to both aspects of rule 10b-5 (although inasmuch as traditional insider trading was clearly illegal anyway, the findings had little bearing on such trading). Trading by informed corporate insiders and trading by those with misappropriated information are both, in the terms of the statute, “trading while in possession of material non-public information,” and thus covered by the terms of the findings. On all accounts, the 1988 Act was supposed to validate rule 14e-3 and the misappropriation doctrine.
IV. THE EFFECT OF THE 1988 FINDINGS

If there is any argument about the 1988 Act's findings, it is probably over whether they are entitled to judicial respect, not whether they relate to rule 14e-3 and the misappropriation doctrine. Whatever the findings accomplish, they accomplish it with respect to rule 14e-3 and the misappropriation doctrine under rule 10b-5. The findings expressly establish the validity of rule 14e-3 and the misappropriation doctrine, and they are Congress's most recent enactment on the subject. Indeed, under the Supreme Court's literalist approach to the securities laws, their language would seem to be more important than the open-ended language of sections 10(b) and 14(e) to the question of the SEC's power to implement the misappropriation doctrine and rule 14e-3. Nevertheless, the courts have so far ignored the 1988 Act's findings. The explanation for this is probably that the courts have not considered the findings; surely no court that knew of the 1988 findings would reject rule 14e-3 and the misappropriation doctrine without at least mentioning them. The Supreme Court did not have to reach the question of the effect of the findings in O'Hagan, because it decided the case before it in the way the findings dictated, albeit without relying upon them. Nevertheless, the findings are relevant to open questions about the scope of the misappropriation doctrine and rule 14e-3. Thus the question remains whether the courts ought to accept the findings as binding.

A. The Legislative Vision of Insider Trading Law

Since the Supreme Court decided United States v. Chiarella, courts and commentators alike have had a hard time fitting insider trading law into the open-ended language of the securities statutes, especially the language of section 10(b) of the Exchange Act. The 1988 Act was enacted more than fifty years after section 10(b), and this Article is not about section 10(b) or about the way the securities laws should have been applied to insider trading before the 1988 Act was enacted. Yet, both the findings and the other provisions of the 1988

105. If the findings are to be read not to encompass rule 14e-3 and the misappropriation doctrine, it has to be on the theory that Congress and the President are held to a very high standard of clarity in writing statutes. Courts generally have not insisted on such a high standard of clarity, and they should be cautious about adopting one now for the securities statutes. See Part IV.B (discussing the appropriateness of using findings to validate a body of judicial and administrative law).

106. See notes 23 and 25 and accompanying text (showing the Court's insistence on the controlling nature of the statutory language).

107. However, Justice Thomas did not mention the findings in his dissent in O'Hagan.
Act are important statements of the current law of insider trading. Perhaps more importantly, the insider trading legislation of the 1980s reflects a vision of the Exchange Act that differs substantially from the vision the Supreme Court offered in its insider trading cases of the early 1980s (and within which lower courts have since been operating). The rules governing insider trading contemplated by this legislative vision may match those contemplated by the judicial vision, but the source of the rules is quite different.

Entirely apart from the 1988 Act, the provisions of the Exchange Act adopted in 1934 can be read to make it illegal to trade securities on the basis of informational advantages that public investors cannot lawfully overcome, and when supplemented by the more recently enacted section 14(e), the pre-1988 Exchange Act can easily support rule 14e-3 as well. The legal rules (including the misappropriation theory) predicted by this interpretation of the pre-1988 statutory regime are entirely consistent with those the Supreme Court adopted in its early insider trading cases, and indeed, the Court approvingly cited the leading exposition of this interpretation of the statute in those cases. In this way of looking at insider trading regulation, the Exchange Act is an independent and self-contained response to a perceived national problem in which federal law operates independently of state law. One might expect to find such a response in one of the great New Deal statutes, but it is not what the Supreme Court seems to have found in its insider trading cases.

The Supreme Court has read section 10(b) as supplementary to and largely derivative of other law, so that it proscribes insider trading only when the trader lies or violates some duty that exists independently of section 10(b).

108. See Victor Brudney, Insiders, Outsiders, and Informational Advantages Under the Federal Securities Laws, 93 Harv. L. Rev. 322, 353-67 (1979) (suggesting that the securities laws prohibit traders from using an informational advantage that public traders cannot overcome); Thel, 42 Stan. L. Rev. at 392-94 (cited in note 12) (suggesting that section 10(b) gives the SEC extremely broad rulemaking power).

109. See Dirks, 463 U.S. at 663-64 (citing Brudney, 93 Harv. L. Rev. at 348 (cited in note 108)).

110. See Part II.A (discussing the scope of § 10(b)); O'Hagan, 1997 U.S. LEXIS 4033 at *21 ("In lieu of premising liability on a fiduciary relationship between company insider and purchaser or seller of the company's stock, the misappropriation theory premises liability on a fiduciary-turned-trader's deception of those who entrusted him with access to confidential information.").
the Court has indicated clearly that some informed traders are subject to duties when they trade, and that breach of those duties results in a violation of rule 10b-5 and section 10(b), neither the source nor the parameters of those duties are clear. The securities statutes do not expressly impose duties in any of the situations in which the Supreme Court has indicated that informed trading does violate section 10(b). The Court has cited common law authorities in its discussion of the duties of informed traders, and perhaps in the Court's view federal insider trading rules are merely particular applications of property or contract rules. However, common law generally did not require even corporate officers to disclose material information before they traded. The Court has never said otherwise concerning the common law, but the source of the duties that it says do bind informed traders remains unclear. In the face of this uncertainty, it is hard to know where to turn to find precisely what those duties are.

Notwithstanding uncertainty about just which duties matter to the Supreme Court, even before the Court decided O'Hagan, most courts enforced the misappropriation doctrine and rule 14e-3, and they justified their decisions within the terms of the Supreme Court's view of the regulatory structure. On the other hand, the Court had occasion to review the misappropriation doctrine and rule 14e-3 because other courts disagreed and concluded that they are inconsistent with what the Supreme Court has said about insider trading. The problem was that the framework the Court established to deal with insider trading in its early cases did not clearly resolve the questions posed by the misappropriation doctrine and rule 14e-3. However, after the Supreme Court spoke on insider trading in the 1980s, Congress specifically addressed insider trading in enacted statutes. In addition to providing sanctions against insider trading, those statutes reflect a different vision of federal securities regulation.

Whatever sections 10(b) and 14(e) meant standing alone in the early 1980s, the federal securities statutes now contain statutorily grounded rules against insider trading. In particular, the 1988 Act amendments to the Exchange Act establish an independent, federal statutory law of insider trading. As the findings show, that law forbids insider trading not only when it runs afoul of the rules set by the Supreme Court in its 1980 insider trading cases, but also if the trad-

111. See Wang and Steinberg, Insider Trading at 1105-78 (cited in note 1) (discussing state law and securities regulation); Bainbridge, 52 Wash. and Lee L. Rev. at 1218-22 (cited in note 12) (discussing the uncertainty of state common law fiduciary duties of officers); Brudney, 93 Harv. L. Rev. at 325 (cited in note 108) (stating that “the common law did not include any such obligation” to disclose as is required by federal law).
ing violates the misappropriation doctrine or rule 14e-3. The Supreme Court has now held that the same result is indicated by its own vision of the securities laws, but the recent statutes suggest an alternative approach to determining what the law is.

To illustrate the substantive difference the 1988 Act makes, consider the question of whether the SEC can regulate insider trading when the trader owes no duty to the person with whom he trades. In its decision in O'Hagan, the Eighth Circuit held that regulation is permissible only when the trader owes such a duty, and this was the premise of its rejection of both the misappropriation doctrine and rule 14e-3. That premise was inconsistent with settled case law anyway, including Supreme Court cases, and now the Court has expressly rejected it. However, Congress rejected it as well, and enacted its rejection. Even the defendant in O'Hagan admitted that the private right of action that the 1988 Act established for contemporaneous traders is available for violations of the misappropriation doctrine.

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113. See Superintendent of Ins. v. Bankers Life & Casualty Co., 404 U.S. 6, 12-13 (1971) (allowing a § 10(b) claim where there is a "sale" of a security and "fraud" in connection with that sale even if the injury is misappropriation of the sale proceeds). The Court essentially rejected the Eighth Circuit's premise in Chiarella, when it indicated that insider selling violates rule 10b-5, inasmuch as insider sellers do not stand in a fiduciary relationship to their buyers until the sale is completed. Chiarella, 443 U.S. at 227 n.8. The Court justified extending the proscription to sellers by quoting Judge Learned Hand (in a case involving section 16 of the Exchange Act and not section 10(b)) to the effect that "it would be a sorry distinction" to regulate insider buying but not selling. Id. (quoting Cody, Roberts & Co., 40 SEC 907, 914, n.23 (1961), quoting Gratz v. Cloughton, 187 F.2d 46, 49 (2d Cir. 1951)). However, the fact that coherence demands that insider selling be treated like insider buying does not mean that insider sellers have a fiduciary duty to their buyers. If they did, corporations presumably would have a fiduciary duty to disclose all material information when they sell securities. Of course, they do not have this duty; if they did, there would have been no reason to enact the Securities Act. Thus, when the Court said that corporate insiders are forbidden to sell on the basis of material nonpublic information, it recognized that insider trading can violate the Exchange Act even if the trader owes no duty to the person with whom she trades.

114. Since the contemporaneous-trader action created by the 1988 Act does not say what is illegal, one might argue that it does not establish that trading on misappropriated information is unlawful, and thus that it does not uncouple the prohibition of insider trading from the existence of a duty to a trading partner. However, section 20(d) of the Exchange Act, 15 U.S.C. § 78t(d) (1994), which was adopted in 1984, expressly makes it unlawful to trade securities while in possession of nonpublic information in a situation in which the trader has no duty to the trading partner. Section 20(d) makes it illegal to trade options while in possession of material nonpublic information if it would be illegal to trade the underlying stock. Yet corporate insiders owe no fiduciary duty to those with whom they trade options in public markets, since their corporations neither issue such options nor have any relationship with their holders. See Wang, 101 Harv. L. Rev. at 1056 n.5 (cited in note 80) ("An insider trader of options may not have such a relationship of "trust and confidence" to the party on the other side of the transaction."). The extension of the insider trading prohibition to insiders who trade options can also be seen as the adoption of a form of the misappropriation theory. See Chestman, 947 F.2d at 578 (Winter, J., concurring in part and dissenting in part) (suggesting that the Insider Trading Sanctions Act of 1984 [which added § 20(d)] "seems premised" on the validity of the misappropriation doctrine).
and numerous commentators had also reached the same conclusion. Indeed, the statute hardly makes sense otherwise.\textsuperscript{116} This statutory remedy is available to plaintiffs who are owed no duty, and thus the remedy uncouples private recovery from the existence of a duty to the private plaintiff. It necessarily contemplates that the violation is not premised on the breach of a duty to the trading partner; the reason the statutory remedy works is that with the 1988 Act, the prohibition of insider trading does not turn on the existence of a duty to the trading partner (if it ever did).

The 1988 Act established the private remedy by statutorily codifying the case law that uniformly held that trading on misappropriated information or in violation of rule 14e-3 was illegal. This law was not grounded in duties to the insider’s trading partner. Recall that while the contemporaneous trading provision of the 1988 Act established a private right of action, it did not say when trading is illegal. Instead it relied on the consistent judicial recognition of the validity of the misappropriation doctrine—documented in the findings—to establish illegality, and moved the law further by adding a private sanction.\textsuperscript{117} Congress took the state of the case law in 1988—which included the misappropriation doctrine and rule 14e-3—and, after codifying that law in the findings, used it as the foundation for its own changes.


\textsuperscript{116} See House Report at 26-27 (cited in note 81). The Committee stated:

\textit{In particular, the codification of a right of action for contemporaneous traders is specifically intended to overturn court cases which have precluded recovery for plaintiffs where the defendant’s violation is premised upon the misappropriation doctrine. . . . . The Committee believes that this result is inconsistent with the remedial purposes of the Exchange Act, and that the misappropriation theory fulfills appropriate regulatory objectives in determining when communicating or trading while in possession of material nonpublic information is unlawful. The bill does not define the term ‘contemporaneous,’ which has developed through case law.}

\textsuperscript{Id. (citations omitted). Many commentators have concluded that the private right of action afforded contemporaneous traders amounts to a ratification of the misappropriation doctrine. See Lengvovort, \textit{Insider Trading} § 6.02 at 6-8 (cited in note 1) (“These legislative histories strongly suggest a congressional endorsement (if not ratification) of the misappropriation theory . . . .”) (citation omitted); Loss and Seligman, \textit{Securities Regulation} at 3653 (cited in note 1) (“Presumably the adoption of § 20A resolves any lingering doubt as to whether there may be private rights of action to enforce the misappropriation theory.”); Bainbridge, 52 Wash. and Lee L. Rev. at 1233 (cited in note 12) (“Congress’s action amounts to an express legislative endorsement of the misappropriation theory.”).}

\textsuperscript{117} Mr. O’Hagan argued that by creating a private right of action for misappropriation in 1988, Congress showed that it did not consider the misappropriation doctrine to be established. Respondent’s Brief in Opposition at 22 (cited in note 115). However, the fact that Congress created a private right of action but did not bother to establish a prohibition suggests that Congress was quite satisfied that misappropriation was already illegal in 1988.
For a more concrete example, consider a question the Supreme Court expressly refused to decide in O'Hagan: whether rule 14e-3 is invalid because it prohibits trading in advance of a tender offer, once a substantial step to commence an offer has been taken. Although the Commission's authority to regulate pre-offer trading might be found to be within its section 14(e) authority to prescribe means reasonably designed to prevent fraudulent or deceptive acts or practices, the 1988 findings provide a complete answer to the question, one that does not require any parsing of deception. Rule 14e-3 by its terms applies to pre-offer trading, and the 1988 Act states that the rule is within the SEC's power.

In O'Hagan, the Supreme Court firmly established the validity of the misappropriation doctrine and rule 14e-3. To this extent, the rules indicated by the currently prevailing judicial vision of insider trading law match those codified in the 1988 Act. However, the law of insider trading is still not settled in all its details. The Court's opinion in O'Hagan certainly suggests a broad construction of the SEC's regulatory power, and perhaps courts faced with novel insider trading questions will follow that lead. So long as they ground their decisions on the open-ended language of sections 10(b) and 14(e), however, they will be subject to the argument that they are making law rather than enforcing the law made by Congress. Indeed, some critics are likely to find fault with the Supreme Court's decision in O'Hagan on this basis. The 1988 findings defuse this argument, however. Indeed, regardless of whether the findings are binding, they clearly indicate that Congress wants the courts and the SEC to enforce rule 14e-3 as written and to continue to enforce the misappropriation doctrine.

B. Are Statutory Findings Binding?

While the Supreme Court's decision in O'Hagan established much of what the 1988 findings were supposed to establish, it left open several questions that the findings might be thought to resolve. Courts dealing with these questions, including the Eighth Circuit on remand of O'Hagan, will thus be left to decide whether to honor the conclusions stated in the findings. Their approach to the question may determine the general efficacy of the statutory technique of enacting what may amount to findings of law.

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119. See notes 6-9 and accompanying text (discussing the Supreme Court's holding in O'Hagan and the questions that the Court did not address).
Although the 1988 findings are structured to accomplish a substantive end—establishing that rule 14e-3 and the misappropriation doctrine are enforceable—they are stated as a congressional discovery, not as an expression of congressional will. The findings do not proscribe anything or purport to change the law. Instead, they essentially approve what the Commission and the courts had done already. This odd approach to statutory drafting leaves the findings open to the charge that they are not substantive legislation within the power of Congress, but instead are merely a statement of congressional opinion without any binding effect on the courts. One might justifiably wonder whether Congress overstepped its power when it enacted that opinion. After all, “[i]t is emphatically the province and duty of the judicial department to say what the law is,”120 and in the findings Congress said that the SEC had acted lawfully.

If the findings were simply a statement by Congress sitting in 1988 about what authority Congress had previously delegated to the SEC, they might be challenged on the theory that Congress had no power to make that statement. That criticism might be mitigated by the fact that the findings were enacted through the constitutionally sanctioned legislative process. “Subsequent legislation declaring the intent of an earlier statute is entitled to great weight in statutory construction,”121 and a case can probably be made that an enacted legislative declaration of the meaning of an earlier statute does bind the courts.122 Fortunately, however, the question of Congress’s power

120. Marbury v. Madison, 5 U.S. (1 Cranch) 137, 177 (1803) (Marshall, C.J.). But see Michael Stokes Paulsen, The Most Dangerous Branch: Executive Power to Say What the Law Is, 83 Geo. L. J. 217, 221-23 (1994) (arguing that each branch of the federal government has power to say what the law is). Professor Paulsen’s argument suggests that Congress has the power to say what its legislation means, but that the courts have power to ignore what Congress says. See id. at 222 (“The result of this interpretative tug-of-war is a decentralized and dynamic model of constitutional interpretation, in which the meaning of the Constitution (and of federal statutes and treaties) is determined, not by any single oracle, but by the interaction of competing viewpoints advanced by different interpreters representing different perspectives.”). See also Printz v. United States, 1997 U.S. LEXIS 4044 at *7-72, 96, 119 (Stevens, J., dissenting) (suggesting that the Supreme Court should respect congressional appraisal of its constitutional power).


122. In addition to saying that it is the duty of the judiciary to say what the law is, Chief Justice Marshall also said that:
to decide in 1988 what it had done in the past need not be answered, since the 1988 findings do not purport to be a statement about what Congress had done in the past, and their force does not depend on their being so characterized.

While statutorily enacted findings are not unusual, enacted findings are an unusual kind of statute. The import of legislative findings has been most fully developed in connection with statutes asserting federal power under the Commerce Clause of the Constitution and the Civil War Amendments.123 Statutes purporting to regulate interstate commerce often recite a congressional finding that the regulated activities affect interstate commerce.124 While the exact weight due such findings is unclear, it is quite clear that courts give them some weight when determining whether a statute is within the federal power.125

Acts in pari materia are to be construed together as forming one act. If in a subsequent clause of the same act provisions are introduced, which show the sense in which the legislature employed doubtful phrases previously used, that sense is to be adopted in construing those phrases. Consequently, if a subsequent act on the same subject affords complete demonstration of the legislative sense of its own language, the rule which has been stated, requiring that the subsequent should be incorporated into the foregoing act, is a direction to courts in expounding the provisions of the law.

Alexander v. Mayor & Commonality of Alexandria, 9 U.S. (5 Cranch) 1, 7-8 (1809). See National R.R. Passenger Corp. v. ICC, 610 F.2d 865 (D.C. Cir. 1979) ("Indeed, [in Alexander] Chief Justice Marshall stated the principle that, if it can be gathered from a subsequent statute in pari materia what meaning the legislature attached to the words of a former statute, this will amount to a legislative declaration of its meaning, and will govern the construction of the first statute.") (quoting Jordan v. Department of Justice, 591 F.2d 753, 770 (D.C. Cir. 1978) (en banc)).


125. See, for example, Perez v. United States, 402 U.S. 146, 154-57 (1971) (reviewing and giving great weight to congressional findings in determining whether loan shark activity can be regulated as interstate commerce); Board of Trade of Chicago v. Olsen, U. S. Attorney, 262 U.S. 1 (1923) (validating Congress's power to pass the Grain Futures Act partly on its use of findings); Laurence H. Tribe, American Constitutional Law § 5-5, at 310-11 (Foundation, 2d ed. 1988) ("In each case, congressional fact-findings stressed that the regulation of local incidents of an activity was necessary to abate a cumulative evil affecting national commerce. The Supreme Court has without fail given effect to such congressional findings."); id. § 5-4 at 308; Jefferson Parish
The 1988 Act's findings would seem to be due at least as much deference as statutory findings on interstate commerce. In a sense, commerce findings are more troubling than the findings of the 1988 Act, for deference to a congressional finding that a particular activity involves interstate commerce works to expand congressional power. Deference to the 1988 findings, on the other hand, would not expand congressional power: Congress clearly has the power to adopt rule 14e-3 and the misappropriation doctrine itself, and no one has suggested that it lacks the power to authorize the SEC to do so. Indeed, the Supreme Court has repeatedly rejected what it considers aggressive SEC claims of authority on the simple basis that Congress never conferred it.

The 1988 Act's findings may differ from the more familiar commerce clause findings in an important sense if they are understood to be findings of law, and not findings of fact. Courts might be especially hostile to legislative findings of law, inasmuch as they would seem to encroach on the judicial power; whereas, statutory findings of a commerce or civil-rights nexus merely seem to encroach on private activity and state power. However, the 1988 findings are no more an encroachment on judicial power than commerce findings

Hospital Dist. v. Hyde, 466 U.S. 2, 10-11 (1984) ("In enacting § 3 of the Clayton Act... Congress expressed great concern about the anticompetitive character of tying arrangements. While this case does not arise under the Clayton Act, the congressional finding made therein concerning the competitive consequences of tying is illuminating, and must be respected.") (citations omitted); Katzenbach v. Morgan, 384 U.S. 641, 653-56 (1966) (upholding Voting Rights Act § 4(e) without explicit statutory findings). Compare City of Bourne v. Flores, 117 S. Ct. 2157, 138 L. Ed. 2d 624 (1997) (discussing judicial deference to congressional conclusions on the propriety of legislation under the Civil War Amendments).

126. The tremendous history of rule 10b-5 litigation and the Supreme Court's willingness to supervise the development of rule 10b-5 jurisprudence indicates that the broad grant of rule-making power implicit in section 10(b) of the Exchange Act does not constitute impermissible delegation to an administrative agency (or to the courts). But see note 96 (discussing Justice Thomas's concerns with the broad delegation of rule-making authority to the SEC as expressed in his dissent in O'Hagan).

127. See, for example, Chiarella, 445 U.S. at 233 ("Formulation of such a broad duty, which departs radically from the established doctrine that duty arises from a specific relationship between two parties... should not be undertaken absent some explicit evidence of congressional intent.").

128. Moreover, Congress might be better than courts at determining facts. See Cox, 80 Harv. L. Rev. at 104-05 (cited in note 123) (asserting congressional competence to find facts). But see Pilchen, 59 Notre Dame L. Rev. at 362-77 (cited in note 123) (arguing that Congress is not necessarily a superior fact-finder). However, it is hard to argue that Congress is better able than courts to find the law. Nonetheless, as discussed below, Congress may be better than the courts at answering the question of the SEC's rulemaking power, and in any event, Congress left the difficult question—when precisely is trading on misappropriated information illegal—for the courts and the SEC. See notes 81 and 83 and accompanying text. Indeed, the difficulty of this question, and Congress's determination to leave it for the courts, probably explains the unusual approach of the 1988 Act.
are. Even though commerce findings are stated as findings of fact, to the extent courts defer to them, they effectively determine matters of law, and, more importantly, work to deprive the courts of much of their power to determine the constitutionality of legislation. If Congress is free to determine the extent to which an activity affects commerce, then the judiciary hardly retains the power to determine the law just because it gets to decide how much of an effect is necessary.\footnote{129}

In any event, the 1988 findings are designed to accomplish something that Congress clearly has the right to do—regulate insider trading. Inasmuch as the findings do not even purport to deprive the courts of the right to say whether Congress has exceeded its constitutional power, they do not infringe on a central judicial function in the way that (binding) findings on the meaning of the Constitution might.\footnote{130}

To be sure, in determining whether the SEC has the power to adopt rule 14e-3 or the misappropriation doctrine, courts had to decide whether Congress authorized their adoption, and it seems that in the findings Congress answered the same question. However, Congress is not forbidden to determine a matter that the courts otherwise would have to determine; that is what Congress does when it enacts commerce findings. The critical question about insider trading law has been whether Congress has delegated rulemaking power to the SEC, and Congress, rather than the courts, delegates regulatory power to the SEC.\footnote{131} Absent the findings, courts have to resort to the (apparently) ambiguous language of sections 10(b) and 14(e) to see what Congress did. The findings may clarify what Congress prohibited or delegated, but if courts are not bound by the findings, it cannot be because Congress cannot say what powers it delegates. Perhaps Congress cannot use enacted findings to delegate power, but if not, it is because of some inherent limit on congressional power, not because findings interfere with or usurp judicial power.\footnote{132}

Even if the 1988 findings are not binding on the courts, they would seem to be due deference under the policies that justify the

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\footnote{129}{See Pilchen, 59 Notre Dame L. Rev. at 377-80, 397 (cited in note 122) (criticizing the fact-law distinction in the context of congressional factfinding).}
\footnote{130}{See id. at 378 ("Marbury's harshest interpretation holds that deciding the constitutionality of statutes is a question of law reserved for the Supreme Court.").}
\footnote{131}{See Merritt, 94 Mich. L. Rev. at 745 (cited in note 123) ("Since the New Deal, the Court has acknowledged that elected legislators, rather than appointed judges, should set economic and social goals in a democratic society.").}
\footnote{132}{The findings may not be binding, however, because of the mechanism Congress used to express itself. See Part IV.B (discussing whether the 1988 findings were binding).}
\end{footnotes}
doctrine of deference to administrative interpretations of statutes that the Supreme Court established in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.* The Supreme Court seems less inclined to defer to the SEC in the interpretation of the securities statutes than it is to defer to other administrative agencies in the interpretation of the statutes they administer. Yet, if considerations of political accountability, expertise, and delegated responsibility indicate that courts should defer to administrative agencies in interpreting statutes, then surely courts should defer to Congress itself.

Perhaps the cases most relevant to the effect and force of the 1988 findings are those in which courts have held that Congress ratified earlier judicial constructions of statutes. If nothing else, the 1988 findings seem to ratify the SEC's adoption of rule 14e-3 and the development of the misappropriation doctrine, or at least the court decisions holding the rule and the doctrine to be enforceable. Although the Supreme Court has been just as hostile to the argument that Congress has ratified lower court securities law decisions as it has been to SEC interpretations of the securities statutes, the Court does accept that at some point congressional ratification of judicial decisions interpreting statutes is binding on the courts.

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134. The Supreme Court has not even cited *Chevron* in any discussions of rule 10b-5, although it did cite *Chevron* in *O'Hagan* when it upheld rule 14e-3. 1997 U.S. LEXIS 4033 at *56. The history of the misappropriation doctrine and rule 14e-3 recounted above, especially the initial acceptance of the doctrine and rule, establish the predicates of *Chevron* deference: that the Exchange Act does not directly speak to SEC's rulemaking power and that the statute can fairly be construed to authorize the SEC to adopt both the doctrine and the rule.
135. See *Red Lion Broadcasting Co.*, 395 U.S. at 380-82 (finding subsequent congressional legislation to vindicate and ratify an earlier FCC interpretation of a statute).
136. See *Central Bank*, 511 U.S. at 188-88 (finding that Congress had not acquiesced in the judicial interpretation of § 10(b) in reenacting the securities laws). But see *Herman & MacLean v. Huddleston*, 459 U.S. 375, 384-85 (1983) (finding support for its construction of § 10(b) in Congress's lack of a response to a line of cases construing § 10(b)).
137. See *Morse*, 116 S. Ct. at 1211-12 (holding that Congress had ratified judicial construction of various provisions of the Voting Right Act); *Curtis v. United States*, 511 U.S. 485, 491-92 (1994) (finding that “Congress's passage of other related statutes" supported the Court's interpretation of the Gun Control Act of 1968); *Herman & MacLean*, 459 U.S. at 384-85 (same); *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 381-82 (1982) (“[T]he fact that a comprehensive reenactment and significant amendment of the [Commodity Exchange Act] left intact the statutory provisions under which the federal courts had implied a cause of action is itself evidence that Congress affirmatively intended to preserve that remedy."; *Flood v. Kuhn*, 407 U.S. 258, 281-283 (1972) (holding that the numerous unsuccessful contrary proposals and the years of “positive inaction” by Congress in the face of judicial decisions so holding went “far beyond mere inference" as to Congress's support and the validity of baseball's antitrust exemption); *Central Bank*, 511 U.S. at 185 (“When Congress reenacts statutory language that has been given a consistent judicial construction, we often adhere to that construction in interpreting the reenacted statutory language.").
When the Supreme Court has rejected the argument that Congress has ratified judicial construction of the securities statutes, it has done so on the explicit holding that Congress in fact has not ratified judicial precedent, not that Congress cannot do so.\textsuperscript{138} The ratification in the enacted 1988 findings, however, is quite explicit. Indeed, it is not hyperbole to say that if ever Congress ratified anything, it ratified the Second Circuit's decisions upholding the misappropriation doctrine and rule 14e-3 with the 1988 findings.\textsuperscript{139} If textualists are concerned with keeping power in Congress acting legislatively and not simply with stymieing government action, they presumably should demand that the findings be respected simply because they are embodied in enacted legislation. Furthermore, the 1988 ratification takes the form of an enacted statute, rather than lying in congressional inaction or committee reports.\textsuperscript{140} Finally, the ratification is unambiguous. The 1988 findings cannot be read as anything but a statement that Congress intended for the misappropriation doctrine and rule 14e-3 to be enforced and to be immune from challenge as beyond the SEC's authority. If the language of the findings is difficult to understand, it is only because of the situation in which they were written, and there is no difficulty in understanding the bottom line.

\textsuperscript{138} See, for example, Central Bank, 511 U.S. at 185-88 (finding that Congress had not reenacted § 10(b) and specifically that Congress had not acquiesced, but not foreclosing Congress's ability to do so).

\textsuperscript{139} See Red Lion Broadcasting Co., 395 U.S. at 380-82. Red Lion held that the FCC properly implemented the fairness doctrine pursuant to its statutory authority to promulgate necessary rules, and presented a situation remarkably similar to that presented by the 1988 findings. According to the Court,

This language [of a 1959 statute requiring that equal time be accorded political candidates but providing that the new requirement created no exception “from the obligation [of licensees] . . . to operate in the public interest and to afford reasonable opportunity for the discussion of conflicting views on issues of public importance”] makes it very plain that Congress, in 1959, announced that the phrase “public interest,” which had been in the Act since 1927, imposed a duty on broadcasters to discuss both sides of controversial public issues. In other words, the amendment vindicated the FCC's general view that the fairness doctrine inhered in the public interest standard. Subsequent legislation declaring the intent of an earlier statute is entitled to great weight in statutory construction. And here this principle is given special force by the equally venerable principle that the construction of a statute by those charged with its execution should be followed unless there are compelling indications that it is wrong, especially when Congress has refused to alter the administrative construction. Here, the Congress has not just kept its silence by refusing to overturn the administrative construction, but has ratified it with positive legislation.

\textsuperscript{140} See Central Bank, 511 U.S. at 186 (“Congress may legislate . . . only through passage of a bill which is approved by both Houses and signed by the President. . . . Congressional inaction cannot amend a duly enacted statute.”) (quoting Patterson v. McLean Credit Union, 491 U.S. 164, 175, n.1 (1989), quoting Johnson v. Transportation Agency, Santa Clara County, 480 U.S. 616, 672 (1987) (Scalia, J., dissenting)).
If the 1988 findings present difficult separation-of-powers problems when they are read as an attempt to bind the courts to hold that rule 14e-3 and the misappropriation doctrine are necessary and proper (and hence enforceable), those problems can be avoided by construing the findings to authorize the SEC to enforce the rule and doctrine or even to enact the rule and doctrine as statutory law. While the 1988 findings are not expressed as a new delegation or a new prohibition, there is no reason that they cannot be treated as such, especially if doing so is necessary to avoid constitutional problems. Congress clearly thought that the rule and doctrine were

141. The findings might also be construed as a delegation of new rulemaking power, as opposed to an authorization to enforce existing (if previously unenforceable) rules. Such a delegation might have created other problems. Every case that had been decided at that time had upheld the SEC’s rulemaking power, and thus however the findings are construed, they did not interfere with the courts’ right to adjudicate pending cases. However, a new authorization in 1988 would have raised the question of the status of existing rules. Clearly, if Congress first had authorized the SEC to adopt rule 14e-3 and the misappropriation doctrine in 1988, the SEC would have had to adopt them before they would be binding on the public. Of course, rules 10b-5 and 14e-3 had already been adopted when the findings were enacted, and an argument that rules 10b-5 and 14e-3 had to be readopted after 1988 before they would have any effect seems excessively formal. Whatever the findings were supposed to accomplish, it is clear that those responsible for them did not contemplate that the rules would have to be readopted before the findings would have any effect. Moreover, as discussed in the text accompanying notes 153-63, in 1988 Congress had good reason to refrain from granting the SEC new rulemaking authority, and it had good reason to understand that it did not need to do so to accomplish the end of immunizing rule 14e-3 and the misappropriation doctrine from the risk of being found beyond the SEC’s authority.

142. If the findings were so construed, they might have created potential retroactivity problems. Suppose, for example, that a trader violated rule 14e-3 before the 1988 Act was enacted but was tried thereafter. A court convinced that the rule had been invalid before the 1988 Act would have had to decide whether the findings had only a prospective effect or whether they were instead a statutory determination that the rule or doctrine had always been within the Commission’s power, and, if the latter were true, whether such a legislative determination was binding on the courts. See Frickey, 46 Case W. Res. L. Rev. at 703-04 (cited in note 123) (discussing relevance of statutory commerce findings to enforcement of earlier statute); Brudney, 93 Mich. L. Rev. at 62 (cited in note 104) (discussing the difficult issues involved with postenactment legislative history); Jill E. Fisch, Retroactivity and Legal Change: An Equilibrium Approach, 110 Harv. L. Rev. 1055 (1997). Compare note 12 (discussing SEC v. Peters, 978 F.2d 1162, 1167 (10th Cir. 1992)).

Before the 1988 Act was enacted, rule 14e-3 and the misappropriation doctrine were well known and had been uniformly upheld. Thus, the situation created by the 1988 Act parallels the situation that exists whenever a court holds that Congress has ratified judicial precedent, although the 1988 Act presents the issue more clearly, since its ratification consists not of congressional silence over time but of a particular act at a definite time. The fact that courts have not been troubled by retroactivity issues in ratification cases suggests that congressional ratification appropriately has retroactive effect or that a ratifying act is simply an authoritative interpretation of an earlier statute. In any event, one of the consequences of the 1988 Act’s having been ignored is that this problem never arose. Eight years have passed since it was enacted, and most transitional problems are presumably moot. Remarkably, however, they may be presented in O’Hagan, since the defendant traded before the 1988 Act was enacted.

143. See Postmaster-General v. Early, 25 U.S. (12 Wheat) 136, 148 (1827) (stating that the words of the statute “perhaps, manifest the opinion of the legislature, that the jurisdiction was in the circuit courts; but ought, we think, to be construed to give it, if it did not previously exist”).
necessary and appropriate law. Congress said as much in the findings and after the findings were enacted, it would have been inappropriate for the SEC to abandon either. Indeed, it might have been illegal.\textsuperscript{44}

\textbf{C. Why Findings?}

Perhaps the problem with the 1988 findings is that Congress employed an inappropriate law-making mechanism. This problem is not the common one that arises when Congress (or a staff member) attempts to legislate through committee reports.\textsuperscript{45} The 1988 findings are part of an enacted statute passed by both houses of Congress and signed by the President, and they are at the front of the statute, where any interested legislator could have seen them. Nevertheless, maybe the findings are legislation but not substantive law. Perhaps, as the Supreme Court said in an early decision rejecting congressional findings, the 1988 findings “do not constitute an exertion of the will of Congress which is legislation, but a recital of considerations which in the opinion of that body existed and justified the expression of its will in the present act.”\textsuperscript{146}

As an initial matter, the findings are not a mere statement of opinion; they serve a substantive purpose in the 1988 Act. The private right of action for contemporaneous traders established by the 1988 Act is clearly a substantive provision, but it is available only when the defendant violates the Exchange Act by trading while in possession of material nonpublic information.\textsuperscript{147} Congress reflected its confidence that insider trading was already illegal when it employed this

\textsuperscript{144} Professor Joseph Grundfest has argued that the SEC has the power to “disimply” the private right of action under rule 10b-5. See Grundfest, 107 Harv. L. Rev. at 965-66 (cited in note 22). I disagree with him, but his work is careful and cannot be rebutted here. The SEC did not create the private right of action for violations of rule 10b-5, and its role in the action's development has been as an adviser to the courts and to Congress. The courts created the private right of action without guidance from Congress, and since then they have accepted primary responsibility for its development, with occasional congressional intervention. See Central Bank, 511 U.S. at 172-78 (stating that “Congress did not create a private § 10(b) cause of action” and subsequently discussing the judicial development of that private action). The 1988 findings, the private rights of action afforded against illegal insider trading in sections 20(d) and 20A of the Exchange Act, and various provisions of the Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737, to be codified at scattered sections of 15 U.S.C., all indicate that Congress takes the existence of a private right of action under rule 10b-5 as a given. If the SEC has only the authority granted it by statute, it would seem to have lost its authority to rescind rule 14e-3 and the misappropriation doctrine when Congress, in a statute, stated that the rules are necessary and appropriate.

\textsuperscript{145} See Brudney, 93 Mich. L. Rev. at 47-60 (cited in note 104) (discussing the arguments against relying on legislative history).

\textsuperscript{146} \textit{Carter v. Carter Coal Co.}, 298 U.S. 238, 290 (1936).

structure for creating a private remedy.\textsuperscript{148} By firmly establishing that insider trading is in fact illegal, the findings ensure that the statutory remedies work.\textsuperscript{149}

Nevertheless, even though the findings have a substantive effect, they are expressed as findings and not as an express command. Reading them in isolation, a legislator deciding whether to vote to enact the findings might not have known what they were supposed to accomplish, beyond endorsing the SEC’s insider trading rules. Yet the fact that the findings may be hard to understand cannot justify ignoring them. Many hard-to-understand statutes are enforceable, and indeed the findings are easier to understand than many other parts of the federal securities statutes. The findings are part of an enacted statute, and enacted statutes are law because they are enacted, not because members of the legislature understand them or want them to be law.

Although the findings by their terms declare the SEC’s insider trading rules to be within the scope of the SEC’s powers, perhaps the findings should have stated their import more clearly. Of course, principles of legislative supremacy, if nothing else, counsel against ignoring a statute,\textsuperscript{150} but perhaps the findings are a special statute that should be ignored.\textsuperscript{151} However, courts have traditionally insisted on especially clear statements of legislative intent only to safeguard

\textsuperscript{148} In contrast, section 20(d) of the Exchange Act, 15 U.S.C. § 78t(d) (1994), which was added in 1984, establishes a private right of action for contemporaneous option traders, but since there was some doubt in 1984 about whether insider trading in options was illegal, section 20(d) also expressly makes such trading illegal.

\textsuperscript{149} See Part III.B (discussing how the findings establish that rule 10b-5 and rule 14e-3 prohibit insider trading).

\textsuperscript{150} But see Thel, 63 Fordham L. Rev. at 1183-84 (cited in note 17) (suggesting that the Supreme Court appropriately could ignore the language of the Securities Act and create its own scheme of private remedies).

\textsuperscript{151} I do not think that the findings can be ignored on the ground that it would have been impossible to assemble a legislative coalition specifically to endorse rule 14e-3 or the misappropriation doctrine. While Congress was not prepared to expand the rules against insider trading in 1988, see House Report at 11 (cited in note 81) ("[T]he Committee does not intend to alter the substantive law of insider trading with this legislation.") , it seems quite clear that it would have enacted an explicit codification of rule 14e-3 and the misappropriation doctrine if doing so had seemed necessary. See Langbein, Insider Trading § 5.02 at 6-6 (cited in note 1) ("Had there been a consensus that current law does not reach such trading [i.e., trading on misappropriated information], there is little doubt that the drafters in either 1984 or 1988 would have attempted to cure the defect. That evidence of legislative intent may well be enough to sustain the theory against claims that it is an ultra vires application of Section 10(b)"); Bainbridge, 52 Wash. & Lee L. Rev. at 1232 n.184 (cited in note 12) (explaining that the Supreme Court’s failure to overrule the misappropriation theory in Carpenter alleviated the need for Congress to define insider trading). As developed in the text, the mechanism of findings recommended itself in 1988 in large part because such an enactment did not appear necessary.
important, constitutionally protected interests. In contrast, the only principle that would justify the Court's insistence on greater clarity here would be the principle that all legislation has to be clear. This is a principle that the Supreme Court has implicitly rejected in every case in which it has applied the notoriously unclear language of section 10(b).

While a rejection of the findings might press Congress to change the way it writes statutes, it would also impose costs on Congress. This imposition might be appropriate if there had been some better statutory technique for establishing the validity of rule 14e-3 and the misappropriation doctrine in 1988. However, given the situation at the time, the findings might have been the best way for Congress to ensure that rule 14e-3 and the misappropriation doctrine would be enforceable.

One alternative approach that Congress sometimes employs to criticize court decisions would not have worked with this statute. Critical findings standing alone presumably would not be held to change the law established by such opinions; moreover, findings are typically accompanied by separate provisions that reverse the law made by the criticized decisions. In the 1988 Act, in contrast, the findings express approval of what the courts had done (and perhaps disapproval of the four unnamed dissenters in United States v. Chestman). Thus, Congress had no occasion to change the law. Nor did it have occasion to restate the law of which it approved. Once again, the critical fact is that when Congress acted, every court that had spoken had upheld the misappropriation doctrine and rule 14e-3. In that situation, legislators who wanted to be sure that the doctrine

152. See Tribe, American Constitutional Law at 182 (cited in note 125) (defending clear statement doctrine that "the amenability of states to suit must be specifically addressed by federal legislation, and Congress must make its intention to treat states like private parties unmistakably clear"); id. at 187 (arguing that the clear statement doctrine structures the legislative process to allow states to protect themselves); id. §§ 5-8, 5-10, 5-20 (discussing the clear statement doctrine and its effect on certain congressional powers); Jonathan R. Macey, Promoting Public-Regarding Legislation Through Statutory Interpretation: An Interest Group Model, 86 Colum. L. Rev. 229, 264-66 (1986) (advocating the use of the "plain meaning rule" in statutory interpretation).

153. See Brudney, 93 Mich. L. Rev. at 20-40 (cited in note 104) (discussing the costs incurred by Congress in clarifying statutory language); Edward O. Correia, A Legislative Conception of Legislative Supremacy, 42 Case W. Res. L. Rev. 1129, 1163 (1992) ("[N]o legislation is cost-free.").

and the rule remained enforceable did not need to enact them into law, because they were already law. All Congress needed was to ensure that the courts did not backpedal, and the findings were an appropriate vehicle for achieving that objective.\textsuperscript{155}

In any event, it would have been very difficult to draft a new statutory grant of rulemaking authority in 1988 that would have permitted the SEC to adopt rule 14e-3 and enforce the misappropriation doctrine.\textsuperscript{156} Sections 10(b) and 14(e) of the Exchange Act already speak in the broadest terms, and it would have been hard to draft a provision giving the Commission greater rule-making power. Even if a broader delegation could have been drafted, enacting it would have risked giving the SEC power to adopt other rules. The 1988 Act was designed to confirm the Commission's power to regulate conduct, not to expand it. A new grant of authority also would have required the Commission to readopt rules 10b-5 and 14e-3, which a Congress fully satisfied with those rules would not have desired, and which might have created a new set of transition problems.\textsuperscript{157} A new grant of authority might also have suggested that the Commission previously had not had authority to adopt the rules, and whatever it intended by the findings, Congress certainly did not intend that result. Finally, and most importantly, Congress had no reason to grant the Commission new authority to adopt rule 14e-3 and the misappropriation doctrine in 1988. Recall that at the time no court had held that the SEC had exceeded its authority: the problem was only a potential one.\textsuperscript{158}

Another way for Congress to protect the misappropriation doctrine and rule 14e-3 would have been to write them into the statute. Yet if Congress wanted to preserve the existing Second Circuit precedent, codification would have been difficult. There were many open questions about the contours of the misappropriation doctrine in 1988, and it probably would have been impossible to put the misappropriation doctrine into statutory terms in 1988.\textsuperscript{159} Moreover, a

\begin{itemize}
\item 155. Nor is it telling that the findings do not refer to the cases they approve by name. There were too many to do so, and in any event the findings endorse the misappropriation doctrine and rule 14e-3, not merely the decisions that had enforced them.
\item 156. See Langevoort, 61 Fordham L. Rev. at S-19 to S-20 (cited in note 22) (discussing reasons why a redrafting of rule 10b-5 is unlikely).
\item 157. See note 141 (discussing the potential problems that a new grant of authority might entail).
\item 158. See Part II.B (discussing the possibility that the SEC exceeded its authority when it passed rule 14e-3).
\item 159. See sources cited in note 51 (discussing open questions in misappropriation doctrine). In this regard, it may be instructive to recall other provisions of the 1988 Act which created increased sanctions for illegal insider trading, but did not say when insider trading was illegal.
\end{itemize}
The statutory definition of insider trading might have discouraged the courts and the SEC from developing the law further and created a roadmap to fraud. 160 An advantage of Congress's technique is that the law of insider trading can continue to evolve through common law adjudication, while assuring that Rule 14e-3 and the floor that the Second Circuit had created in its misappropriation cases remained secure. This is what Congress wanted, 161 and the findings were the best way to accomplish it.

The language, history, and structure of the 1988 Act show that what Congress wanted to do, and thought it was doing, was to protect the misappropriation doctrine and rule 14e-3 from attack. Congress did not want to expand the prohibition of insider trading, but was instead content to allow the SEC to press for further developments in the courts. 162 The findings were not a mere hortatory statement that insider trading is bad. Instead, the findings protected the legal status quo, allowing the law to ratchet toward greater prohibition, but preventing it from falling back. Far from being sloppy, the findings seem carefully crafted, designed to accomplish just what was needed in 1988, and no more. It is particularly telling that the most influential scholars of securities law, Professors Louis Loss and Joel Seligman, wrote in 1991 that most of the anomalies of insider trading law could be remedied by enacting into law a version of the misappropriation theory and rule 14e-3. 163 The 1988 findings, which they too ignore, were just that enactment.

V. CONCLUSION

The debate over the SEC's power to regulate insider trading has been one of the most difficult and contentious of corporate law. Courts have controlled this debate by insisting that the SEC cannot

160. See note 83 and accompanying text (explaining why Congress did not provide a definition of insider trading in the 1988 Act).
161. See notes 90 and 151 and accompanying text (discussing the application and the role of Rule 10b-5 and Rule 14e-3).
162. The House Committee Report on the 1988 Act indicated that the Committee did not intend to alter the law of insider trading. House Report at 11 (cited in note 81). At the same time, the findings themselves make clear that Congress did not want to see the law roll back. The minority (Republican) counsel to the House Committee on Energy and Commerce subsequently wrote that the findings were enacted to assist the SEC in its efforts to bring insider trading cases. Kaswell, 45 Bus. Law. at 157 (cited in note 129) ("The Committee wanted to draft legislation that would assist the SEC in its efforts to bring insider trading cases; at the same time, the Committee decided that it did not wish to create a definition of that offense or alter the substantive law of insider trading.").
163. Loss and Seligman, 8 Securities Regulation at 3770 (cited in note 1).
expand its attack on insider trading until Congress speaks to the question. In 1988, Congress did address the SEC's power to regulate insider trading. This statement might seem flawed and unworthy of respect, but on careful examination it appears extremely well-constructed to establish the validity of the misappropriation doctrine and rule 14e-3. If it employed an unusual structure, it did so because of the confused state of insider trading law when it was enacted, confusion for which the courts were largely responsible. The judge-made law of rule 10b-5 has already largely supplanted enacted statutes as the primary vehicle of securities regulation. If Congress cannot construct securities legislation on the assumption that firmly established judge-made law in fact is settled, it will be hard pressed to participate in the lawmaking process at all. In any event, courts that insist it is up to Congress to make law should not ignore the law Congress has made.