NASD

Notice To Members

National Association of Securities Dealers, Inc. January 1989

Number 89-1

Suggested Routing:*

✓Senior Management	__Internal Audit	__Operations	__Syndicate
__Corporate Finance	✓Legal & Compliance	__Options	__Systems
__Government Securities	__Municipal	__Registration	__Trading
__Institutional	__Mutual Fund	__Research	__Training

*These are suggested departments only. Others may be appropriate for your firm.

IMPORTANT MAIL VOTE

Subject: Proposed By-Laws Amendment on Filling Vacancies on District Committees; Last Voting Date: February 3, 1989

EXECUTIVE SUMMARY

The NASD invites members to vote on a proposed amendment to Article VIII, Section 5 of the NASD By-Laws that would expedite the filling of vacancies created by departures of District Business Conduct Committee (DBCC) members during their terms and avoid the necessity of holding interim elections.

The amendment would provide for appointment of a person by the remaining DBCC members to fill the departing Committee member's seat until the next regularly scheduled election. At that time, the normal election process would occur to elect a new Committee member to serve for the duration of the departing Committee member's term.

The text of the proposed amendment follows this notice.

BACKGROUND AND SUMMARY

The NASD Board of Governors is concerned about practical problems encountered by District Committees when vacancies on a DBCC occur as a result of departures of Committee members during their terms. Such problems, including the necessity for holding special interim elections, would be alleviated by the proposed amendment to Article VIII, Section 5 of the NASD By-Laws.

The current procedure under Sections 5(a) and (b) of Article VIII of the NASD By-Laws sets forth a two-step mechanism for filling vacancies on a DBCC. If the unexpired term of the Committee member causing the vacancy is less than 12 months, the vacancy is to be filled by appointment by the remaining members of the DBCC of a representative of a member firm having a place of business in the same district. If the unexpired term of the Committee member causing the vacancy is 12 months or more, the vacancy is to be filled by election conducted in accordance with the provisions of Section 4 of Article VIII.

The Board of Governors believes that the current procedure requiring the holding of interim elections is burdensome and unnecessary. The Board, upon the recommendation of the Advisory Council and the National Business Conduct Committee, is therefore proposing to eliminate the requirement for a special election to be conducted to fill a vacancy of 12 months or more. Instead, regardless of the length of the remaining term, the

remaining members of the DBCC would appoint a representative of a member firm doing business in the same district to fill the departing Committee member's seat until the next regularly scheduled election. A new Committee member would then be elected to serve for the duration of the departing Committee member's term.

In so proposing, the Board recommends that, in each instance, the DBCC should seriously consider former DBCC members for appointment to a vacancy. Because of prior experience, such persons would be able to assume such a position and make a meaningful contribution.

Therefore, the Board of Governors has approved the proposed amendment to Article VIII, Section 5 of the NASD By-Laws, and the amendment now is being submitted for membership approval. Prior to becoming effective, the By-Laws change also must be approved by the Securities and Exchange Commission.

COMMENTS RECEIVED

The proposed amendment to Article VIII, Section 5 of the NASD By-Laws was published for comment in NASD Notice to Members 88-48, dated July 1988. The NASD received three comments on the proposed amendment — two in opposition, and one in favor.

The negative comments generally questioned the NASD's argument that interim elections are too expensive; expressed concern that appointees would be obligated to the Committee and thus not maintain sufficient independence; and opined that the present system provides more persons with an opportunity to serve on a DBCC. The Board considered these issues and determined that the proposed amendment is appropriate since interim elections are an unnecessary expense, both monetarily and in terms of disruption of district operations. Further, DBCC members have been exercising appointive power in situations where the unexpired term of the departing Committee member is less than 12 months and the appointee would fill the vacancy only until the next scheduled election.

The Board of Governors thus believes that the proposed amendment to Article VIII, Section 5 of the NASD By-Laws is necessary and appropriate and recommends that members vote their approval.

Please mark the attached ballot according to your convictions and return it in the enclosed, stamped envelope to The Corporation Trust Company.

Ballots must be postmarked **no later than February 3, 1989.**

Questions concerning this notice can be directed to Deborah F. McIlroy, Attorney, NASD Office of General Counsel, at (202) 728-8816.

PROPOSED AMENDMENT TO ARTICLE VIII, SECTION 5 OF THE NASD BY-LAWS

(**Note:** New text is underlined; deleted text is in brackets.)

Filling of Vacancies on District Committees

Sec. 5. All vacancies in any District Committee other than those caused by the expiration of a Committee [m]Member's term of office shall be filled as follows:

[(a) If the unexpired term of the member causing the vacancy is for less than twelve months, such vacancy shall be filled by appointment by the remaining members of the District Committee of some member of the Corporation having a place of business in the same district.

(b) If the unexpired term of the member causing the vacancy is for twelve months or more, such vacancy shall be filled by election, which shall be conducted as nearly as practicable in accordance with the provisions of Section 4 of this Article.]

The District Committee shall appoint a representative of a member firm having a place of business in the same district to fill any vacancy resulting from the unexpired term of a departed Committee Member. Such appointment shall be effective until the next regularly scheduled election occurs, in accordance with the provisions of Section 4 of this Article. Following this election, the newly elected Committee Member will serve only the duration of the departed Committee Member's term.

NASD

Notice To Members

National Association of Securities Dealers, Inc. January 1989

Number 89-2

Suggested Routing:*

✓Senior Management	__Internal Audit	✓Operations	__Syndicate
__Corporate Finance	✓Legal & Compliance	__Options	__Systems
__Government Securities	__Municipal	__Registration	✓Trading
__Institutional	__Mutual Fund	__Research	__Training

*These are suggested departments only. Others may be appropriate for your firm.

IMPORTANT MAIL VOTE

Subject: Proposed New Rule Regarding Business Conduct of Members;
Last Voting Date: February 3, 1989

EXECUTIVE SUMMARY

Members are invited to vote on a proposed new Section 44 to Article III of the NASD Rules of Fair Practice that would prevent a firm that withdraws or is removed as a market maker in a NASDAQ security from continuing market-making activity in that security in the over-the-counter market during any period that the member is ineligible to re-enter NASDAQ as a market maker.

The text of the proposed rule follows this notice.

BACKGROUND AND ANALYSIS

On June 9, 1988, the SEC approved amendments to the Rules of Practice and Procedures for the Small Order Execution System (SOES Rules) and to Schedule D to the NASD By-Laws. The amended rules, in part, require that a market maker in a NASDAQ National Market System (NASDAQ/NMS) security also be registered as a market maker in SOES with respect to that security. In addition, the amended SOES Rules impose a penalty of 20 business days for unexcused withdrawal from market making in any NASDAQ security. As noted in the SEC's order approving the SOES amendments, the amendments are "designed to improve the accuracy of quotations displayed through the NASDAQ System, and to enhance the liquidity of the over-the-counter (OTC) market by increasing the level of participation of NASDAQ market makers in SOES."[1]

The NASD believes that the public-policy purpose behind the adoption of the SOES amendments in June 1988 would be undermined if firms could readily withdraw from making a market in a NASDAQ security and transfer their market-making activity to the non-NASDAQ OTC market during the 20-business-day penalty period.

The proposed amendment prohibits firms that make a market in a NASDAQ security from transferring their market-making activity in that NASDAQ security to the non-NASDAQ OTC market during any period in which the firm is ineligible to re-enter the NASDAQ System as a market maker.

The NASD Board of Governors believes that the proposed rule amendment helps to preserve the viability of the SOES system because market makers will not be able to avoid the 20-business-day penalty provision by transferring their market-making activity to the OTC market

during that time. Thus, the Board believes that the proposed amendments are necessary and appropriate and recommends that members vote their approval.

Please mark the attached ballot according to your convictions and return it in the enclosed, stamped envelope to The Corporation Trust Company. Ballots must be postmarked **no later than February 3, 1989.**

Questions concerning this notice may be directed to Eneida Rosa, Assistant General Counsel, NASD Office of General Counsel, at (202) 728-8284.

PROPOSED AMENDMENT TO ARTICLE III, RULES OF FAIR PRACTICE

(Note: New language is underlined.)

Business Conduct of Members
Sec. 44

A member that has withdrawn from participation in the NASDAQ System as a market maker in any NASDAQ security pursuant to the provisions of Part VI, Section 8 of Schedule D to the NASD By-Laws shall not act as a market maker in that security in the over-the-counter market during any period that the member is ineligible to re-enter NASDAQ as a market maker.

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[1] File No. SR-NASD-88-1, Securities Exchange Act Release No. 25791 (June 9, 1988).

NASD

Notice To Members

National Association of Securities Dealers, Inc. January 1989

Number 89-3

Suggested Routing:*

✓Senior Management	✓Internal Audit	✓Operations	__Syndicate
__Corporate Finance	✓Legal & Compliance	__Options	__Systems
__Government Securities	__Municipal	__Registration	__Trading
__Institutional	__Mutual Fund	__Research	__Training

*These are suggested departments only. Others may be appropriate for your firm.

REQUEST FOR COMMENTS

Subject: Proposed Rule to Restrict Payment of Referral Fees by NASD Members;
Last Date for Comments: February 3, 1989

EXECUTIVE SUMMARY

The NASD invites comments on a proposed rule that would restrict the payment of "finders" or referral fees by NASD members to unregistered third parties for the referral of retail business. Fees paid in connection with a member's underwriting or merger-and-acquisition business would be excluded from the purview of the Rule, which also would permit an occasional fixed-amount referral-fee payment under certain circumstances. The text of the proposed rule follows this notice.

BACKGROUND

The NASD consistently has taken the position that it is improper for a member or a person associated with a member to make payments of "finders" or referral fees to third parties who introduce or refer prospective brokerage customers to the firm. This position is based on the definition of "representative" set forth in Part III (1)(b) of Schedule C to the NASD By-Laws, which states:

> Persons associated with a member . . . who are engaged in the investment banking or securities business for the member including the functions of supervision, solicitation or conduct of business in securities . . . are designated as representatives. (Emphasis added.)

The NASD has maintained that persons who introduce or refer prospective customers and receive compensation for such activities are engaged in the securities business for the member in the form of solicitation. Solicitation is the first step in the consummation of a securities transaction and must be regarded as part of the conduct of business in securities. Although the NASD, on an informal basis, has permitted "one-time" fees not tied to the completion of a transaction or the opening of an account, it has, as noted above, consistently taken the position that the activities of locating, introducing, or referring potential retail customers come within the definition of representative and that those persons performing such activities are acting on behalf of the member.

The NASD has noted an increasing number of inquiries regarding the propriety of paying referral fees. To clarify the NASD's position and make it available to all members, the Qualifications Committee recommended, and the Board of

Governors approved, the publication for comment of the proposed rule.

ANALYSIS OF PROPOSED AMENDMENT

The proposed Rule of Fair Practice regarding referral fees generally would prohibit payment of compensation to individuals or business entities for the referral of potential customers for brokerage services. Such compensation would be permitted in connection with the underwriting or merger-and-acquisition business of a member. In addition, members would be permitted to pay fixed fees for referrals on an occasional basis, provided that the fee is minimal and that neither the entitlement to nor the amount of the fees are linked to the opening of an account, the execution of transactions, the volume of business, or in any other way tied to the outcome of the referral. The payment of referral fees by associated persons would be prohibited under any circumstance.

The NASD believes that it is important to be able to regulate the flow of securities-related compensation from its members to unregistered persons. The Board of Governors believes that a Rule of Fair Practice, as described above, would significantly reduce the risks attendant on the solicitation of securities transactions by unregistered persons, while providing for the payment of referral fees under certain circumstances, such as the purchase of a mailing list, that do not pose such risks.

The NASD encourages all members and interested parties to comment on the proposed Rule of Fair Practice. Comments should be directed to

Mr. Lynn Nellius, Secretary
National Association of Securities Dealers, Inc.
1735 K Street, NW
Washington, DC 20006-1506

Comments must be received **no later than February 3, 1989**. Comments received by this date will be considered by the Qualifications Committee and the Board of Governors. The proposed Rule of Fair Practice must be approved by the membership and filed with, and approved by, the SEC before becoming effective.

Questions concerning this notice can be directed to Dennis C. Hensley, NASD Vice President and Deputy General Counsel, at (202) 728-8245, or Frank J. McAuliffe, NASD Vice President, Qualifications, at (301) 590-6694.

PROPOSED AMENDMENT TO NASD RULES OF FAIR PRACTICE

(a) No member or person associated with a member shall, directly or indirectly, give or permit to be given to any individual or business enterprise (other than persons registered with the member and other members) compensation of any kind in connection with the referral of prospective customers to the member.

(b) Paragraph (a) shall not apply to:

(1) the payment of compensation for the referral of business by a member where the compensation is solely in connection with the underwriting or merger and acquisition business of the member;

(2) the payment by a member of a fixed fee for the purchase of a listing of prospective customers; and

(3) the payment by a member of a small fixed fee for a referral where the payment is occasional, not part of a pattern or practice of such payments to the recipient, not determined by the outcome of the referral, and where the recipient does not regularly engage in activity that might reasonably be expected to result in continued referrals.

NASD

Notice To Members

National Association of Securities Dealers, Inc. January 1989

Number 89-4

Suggested Routing:*

- ✓ Senior Management
- ✓ Internal Audit
- ✓ Operations
- __ Syndicate
- __ Corporate Finance
- ✓ Legal & Compliance
- __ Options
- ✓ Systems
- __ Government Securities
- __ Municipal
- ✓ Registration
- __ Trading
- __ Institutional
- __ Mutual Fund
- __ Research
- __ Training

*These are suggested departments only. Others may be appropriate for your firm.

REQUEST FOR COMMENTS

Subject: Proposed Mandatory Participation by Clearing Members in Reconfirmation and Pricing Services (RECAPS); Last Date for Comment: February 3, 1989

EXECUTIVE SUMMARY

The NASD is requesting comment on a proposed new Section 69 to the Uniform Practice Code. The new section would require that all NASD members that are participants in a registered clearing agency for purposes of clearing OTC transactions must participate in fail reconfirmation and pricing services if offered by the respective clearing agency of which they are a member.

BACKGROUND

In June 1987, the National Securities Clearing Corporation (NSCC), at the request of various industry groups, offered to its participants a new service, Re-Confirmation and Pricing Service (RECAPS). The service allowed NSCC participants the ability to reconfirm open aged fails, reprice such fails to the current market and, where possible, net the reconfirmed and repriced fails. The original service limited its scope to aged municipal bond fails.

Since that time, RECAPS has been expanded to allow the submission of over-the-counter equity securities and zero-coupon instruments (CATS/TIGRS). Aged fails in these eligible securities may be submitted for RECAPS through NSCC even though the original settlement occurred "ex-clearing." CNS-eligible recompared fails are forwarded to CNS for processing and settlement; non-CNS-eligible issues are netted, where applicable, and balance orders generated. RECAPS now is offered solely to NSCC participants, and its usage is on a voluntary basis.

The NASD's Uniform Practice Committee, upon the recommendation of its Operations Sub-Committee, reviewed NSCC's enhanced RECAPS and determined that such reconfirmation and pricing services offer major operational and financial benefits to their users with minimal additional staffing requirements. Specifically, fail updating and repricing (to the current market value) affords protection against market fluctuations.

Additionally, original contractual commitments are either affirmed or identified as problem items needing more attention. Also of importance is the establishment of a new settlement date that alleviates potential capital charges pursuant to the uniform net capital rule as they apply to aged fails.

EXPLANATION

The proposed new Section 69 of the Uniform

Practice Code would require members who are participants in a registered clearing agency offering reconfirmation and pricing services to submit for RECAPS processing their aged fails in eligible securities that are subject to the provisions of the Uniform Practice Code. Further, Section 59 will be amended to provide protection for members against potential liability or losses that might arise when a buy-in is pending during a RECAPS processing cycle.

The NASD encourages all members and other interested parties to comment on the proposed new Section 69 of the Uniform Practice Code. Comments should be directed to:

Mr. Lynn Nellius, Secretary
National Association of Securities Dealers, Inc.
1735 K Street, NW
Washington, DC 20006-1506

Questions concerning this notice can be directed to Donald J. Catapano, NASD Uniform Practice/TARS at (212) 858-4350.

PROPOSED NEW SECTION TO THE UNIFORM PRACTICE CODE

Reconfirmation and Pricing Service Participation

Section 69

Each member or its agent that is a participant in a registered clearing agency, for purposes of clearing over-the-counter securities transactions, shall participate in fail reconfirmation and pricing services when offered.

NASD

Notice To Members

National Association of Securities Dealers, Inc. January 1989

Number 89-5

Suggested Routing:*

- ✓ Senior Management
- ✓ Corporate Finance
- __ Government Securities
- __ Institutional
- __ Internal Audit
- ✓ Legal & Compliance
- __ Municipal
- __ Mutual Fund
- ✓ Operations
- __ Options
- __ Registration
- __ Research
- __ Syndicate
- __ Systems
- ✓ Trading
- ✓ Training

*These are suggested departments only. Others may be appropriate for your firm.

Subject: Insider Trading and Securities Fraud Enforcement Act of 1988

EXECUTIVE SUMMARY

Congress passed the Insider Trading and Securities Fraud Enforcement Act of 1988, which became effective on November 19, 1988, and augments enforcement of the securities laws, particularly in the area of insider trading.

The full text of the legislation follows this notice.

BACKGROUND

On September 14, 1988, Congress approved the Insider Trading and Securities Fraud Enforcement Act of 1988 ("the Act"). It augments enforcement of the securities laws, particularly in the area of insider trading, through a variety of measures designed to provide greater deterrence, detection, and punishment of insider-trading violations and other perceived market abuses.

The legislation became effective when it was signed by President Reagan November 19, 1988. This notice provides members with a summary of some of the pertinent provisions under this Act (Public Law 704). Members and associated persons should consult with their counsel to ensure that their trading activities comply with the requirements of this Act.

PROVISIONS UNDER THE INSIDER TRADING AND SECURITIES FRAUD ENFORCEMENT ACT

Some of the pertinent provisions are as follows:

■ **Controlling Persons**

Through additions to the Securities Exchange Act of 1934, the civil penalties for insider traders and controlling persons are broadened. The legislation extends liability to firms or other "controlling persons" who knowingly or recklessly fail to take the appropriate measures to prevent the occurrence of insider-trading violations. Controlling persons must establish, maintain, and enforce written policies and procedures "reasonably designed" to guard against insider trading. Interpretation of "controlling persons" will be done on a case-by-case basis, and may include not only employers, but any person with power to influence or control the direction of the management, policies, or activities of another person.

■ **Penalties**

Civil: The SEC may impose damages against violators for three times the profit gained or loss avoided and not more than $1,000,000 for controlling persons.

Criminal:

Individuals — Maximum fine increased from $100,000 to $1,000,000.

Non-natural — Maximum fine increased from $500,000 to $2,500,000.

Jail sentences — Maximum term increased from five to 10 years.

The legislation makes all non-natural persons subject to the higher criminal penalty.

■ **Class of Traders**

Contemporaneous —The Act codifies an express private right of action for those who traded in the same class of securities "contemporaneously" with the insider trader and not to an endless string of "tippees."

Non-contemporaneous — Despite the absence of explicit statutory language, the Act relies on the flexibility of Section 10(b) of the Exchange Act to provide an "implied private cause of action" for certain non-contemporaneous traders. For example, this right would extend to those who must pay more for a target company because insider trading forced up the price of a target's stock.

■ **Foreign Assistance**

Provisions have been incorporated in the Act that allow the SEC, at its discretion, to provide assistance to foreign governments in connection with gathering information regarding alleged violations of foreign securities laws.

■ **SEC Study**

Contingent on the appropriation of funds, the Act directs the SEC to study the adequacy of the federal securities laws.

■ **Bounty Provision**

The Act authorizes the SEC to award bounty payments of up to 10 percent of the civil penalty imposed to persons who provide information regarding insider-trading violations.

■ **Statute of Limitations**

No action may be brought more than five years after the date of the last transaction that is the subject of the violation.

■ **SEC Recommendations**

Within 60 days of enactment, the SEC must give Congress recommendations regarding its authority to impose civil penalties in areas other than insider trading.

INSIDER TRADING AND SECURITIES FRAUD ENFORCEMENT ACT OF 1988

Section 1. SHORT TITLE.

This Act may be cited as the "Insider Trading and Securities Fraud Enforcement Act of 1988."

Section 2. FINDINGS.

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, nonpublic 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.

Section 3. CIVIL PENALTIES OF CONTROLLING PERSONS FOR ILLEGAL INSIDER TRADING BY CONTROLLED PERSONS.

(a) AMENDMENT — The Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.) is amended —

(1) in section 21(d) —

(A) by striking out paragraph (2); and

(B) by redesignating subsection (d)(1) as subsection (d); and

(2) by inserting after section 21 the following new section:

CIVIL PENALTIES

Section 21A. (a) AUTHORITY TO IMPOSE CIVIL PENALTIES. —

(1) JUDICIAL ACTIONS BY COMMISSION AUTHORIZED. — Whenever it shall appear to the Commission that any person has violated any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information in, or has violated any such provision by communicating such information in connection with, a transaction on or through the facilities of a national securities exchange or from or through a broker or dealer, and which is not part of a public offering by an issuer of securities other than standardized options, the Commission —

(A) may bring an action in a United States district court to seek, and the court shall have jurisdiction to impose, a civil penalty to be paid by the person who committed such violation; and

(B) may, subject to subsection (b)(1), bring an action in a United States district court to seek, and the court shall have jurisdiction to

impose, a civil penalty to be paid by a person who, at the time of the violation, directly or indirectly controlled the person who committed such violation.

(2) AMOUNT OF PENALTY FOR PERSON WHO COMMITTED VIOLATION. — The amount of the penalty which may be imposed on the person who committed such violation shall be determined by the court in light of the facts and circumstances, but shall not exceed three times the profit gained or loss avoided as a result of such unlawful purchase, sale, or communication.

(3) AMOUNT OF PENALTY FOR CONTROLLING PERSON. — The amount of the penalty which may be imposed on any person who, at the time of the violation, directly or indirectly controlled the person who committed such violation, shall be determined by the court in light of the facts and circumstances, but shall not exceed the greater of $1,000,000, or three times the amount of the profit gained or loss avoided as a result of such controlled person's violation. If such controlled person's violation was a violation by communication, the profit gained or loss avoided as a result of the violation shall, for purposes of this paragraph only, be deemed to be limited to the profit gained or loss avoided by the person or persons to whom the controlled person directed such communication.

(b) LIMITATIONS ON LIABILITY. —

(1) LIABILITY OF CONTROLLING PERSONS. — No controlling person shall be subject to a penalty under subsection (a)(1)(B) unless the Commission establishes that —

(A) such controlling person knew or recklessly disregarded the fact that such controlled person was likely to engage in the act or acts constituting the violation and failed to take appropriate steps to prevent such act or acts before they occurred; or

(B) such controlling person knowingly or recklessly failed to establish, maintain, or enforce any policy or procedure required under section 15(f) of this title or section 204A of the Investment Advisers Act of 1940 and such failure substantially contributed to or permitted the occurrence of the act or acts constituting the violation.

(2) ADDITIONAL RESTRICTIONS ON LIABILITY. — No person shall be subject to a penalty under subsection (a) solely by reason of employing another person who is subject to a penalty under such subsection, unless such employing person is liable as a controlling person under paragraph (1) of this subsection. Section 20(a) of this title shall not apply to actions under subsection (a) of this section.

(c) AUTHORITY OF COMMISSION. — The Commission, by such rules, regulations, and orders as it considers necessary or appropriate in the public interest or for the protection of investors, may exempt, in whole or in part, either unconditionally or upon specific terms and conditions, any person or transaction or class of persons or transactions from this section.

(d) PROCEDURES FOR COLLECTION. —

(1) PAYMENT OF PENALTY TO TREASURY. — A penalty imposed under this section shall (subject to subsection (e)) be payable into the Treasury of the United States.

(2) COLLECTION OF PENALTIES. — If a person upon whom such a penalty is imposed shall fail to pay such penalty within the time prescribed in the court's order, the Commission may refer the matter to the Attorney General who shall recover such penalty by action in the appropriate United States district court.

(3) REMEDY NOT EXCLUSIVE. — The actions authorized by this section may be brought in addition to any other actions that the Commission or the Attorney General are entitled to bring.

(4) JURISDICTION AND VENUE. — For purposes of section 27 of this title, actions under this section shall be actions to enforce a liability or a duty created by this title.

(5) STATUTE OF LIMITATIONS. — No action may be brought under this section more than 5 years after the date of the purchase or sale. This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this title, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties, imposed in an action commenced within 5 years of such transaction.

(e) AUTHORITY TO AWARD BOUNTIES TO INFORMANTS. — Notwithstanding the provisions of subsection (d)(1), there shall be paid from amounts imposed as a penalty under this section and recovered by the Commission or the Attorney General, such sums, not to exceed 10 percent of such amounts, as the Commission deems appropriate, to the person or persons who provide information leading to the imposition of such penalty. Any determinations under this subsection including whether, to whom, or in what amount to make payments, shall be in the sole discretion of the Commission, except that no such payment shall be made to any member, officer, or employee of any appropriate regulatory agency, the Department of

Justice, or a self-regulatory organization. Any such determination shall be final and not subject to judicial review.

(f) DEFINITION. — For purposes of this section, "profit gained" or "loss avoided" is the difference between the purchase or sale price of the security and the value of that security as measured by the trading price of the security a reasonable period after public dissemination of the nonpublic information.

(b) AMENDMENTS CONCERNING SUPERVISION. —

(1) BROKERS AND DEALERS. — Section 15 of the Securities Exchange Act of 1934 (15 U.S.C. 780) is amended by adding at the end thereof the following new subsection:

(f) Every registered broker or dealer shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such broker's or dealer's business, to prevent the misuse in violation of this title, or the rules or regulations thereunder, of material, nonpublic information by such broker or dealer or any person associated with such broker or dealer. The Commission, as it deems necessary or appropriate in the public interest or for the protection of investors, shall adopt rules or regulations to require specific policies or procedures reasonably designed to prevent misuse in violation of this title (or the rules or regulations thereunder) of material, nonpublic information.

(2) INVESTMENT ADVISERS. — The Investment Advisers Act of 1940 (15 U.S.C. 80b-1 et seq.) is amended by adding after section 204 the following new section:

PREVENTION OF MISUSE OF NONPUBLIC INFORMATION

Section 204A. Every investment adviser subject to section 204 of this title shall establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such investment adviser's business, to prevent the misuse in violation of this Act or the Securities Exchange Act of 1934, or the rules or regulations thereunder, of material, nonpublic information by such investment adviser or any person associated with such investment adviser. The Commission, as it deems necessary or appropriate in the public interest or for the protection of investors, shall adopt rules or regulations to require specific policies or procedures reasonably designed to prevent misuse in violation of this Act or the Securities Exchange Act of 1934 (or the rules or regulations thereunder) of material, nonpublic information.

(c) COMMISSION RECOMMENDATIONS FOR ADDITIONAL CIVIL PENALTY AUTHORITY REQUIRED. — The Securities and Exchange Commission shall, within 60 days after the date of enactment of this Act, submit to each House of the Congress any recommendations the Commission considers appropriate with respect to the extension of the Commission's authority to seek civil penalties or impose administrative fines for violations other than those described in section 21A of the Securities Exchange Act of 1934 (as added by this section).

Section 4. INCREASES IN CRIMINAL PENALTIES.

Section 32(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78ff(a)) is amended —

(1) by striking "$100,000" and inserting "$1,000,000";

(2) by striking "five years" and inserting "10 years";

(3) by striking "is an exchange" and inserting "is a person other than a natural person"; and

(4) by striking out "$500,000" and inserting "$2,500,000."

Section 5. LIABILITY TO CONTEMPORANEOUS TRADERS FOR INSIDER TRADING.

The Securities Exchange Act of 1934 is amended by inserting after section 20 the following new section:

LIABILITY TO CONTEMPORANEOUS TRADERS FOR INSIDER TRADING

Section 20A. (a) PRIVATE RIGHTS OF ACTION BASED ON CONTEMPORANEOUS TRADING . — Any person who violates any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

(b) LIMITATIONS ON LIABILITY. —

(1) CONTEMPORANEOUS TRADING ACTIONS LIMITED TO PROFIT GAINED OR LOSS AVOIDED. — The total amount of damages imposed under subsection (a) shall not exceed the profit gained or loss avoided in the transaction or

transactions that are the subject of the violation.

(2) OFFSETTING DISGORGEMENTS AGAINST LIABILITY. — The total amount of damages imposed against any person under subsection (a) shall be diminished by the amounts, if any, that such person may be required to disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 21(d) of this title relating to the same transaction or transactions.

(3) CONTROLLING PERSON LIABILITY. — No person shall be liable under this section solely by reason of employing another person who is liable under this section, but the liability of a controlling person under this section shall be subject to section 20(a) of this title.

(4) STATUTE OF LIMITATIONS. — No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

(c) JOINT AND SEVERAL LIABILITY FOR COMMUNICATING. — Any person who violates any provision of this title or the rules or regulations thereunder by communicating material, nonpublic information shall be jointly and severally liable under subsection (a) with, and to the same extent as, any person or persons liable under subsection (a) to whom the communication was directed.

(d) AUTHORITY NOT TO RESTRICT OTHER EXPRESS OR IMPLIED RIGHTS OF ACTION. — Nothing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this title or the availability of any cause of action implied from a provision of this title.

(e) PROVISIONS NOT TO AFFECT PUBLIC PROSECUTIONS. — This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this title, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties."

Section 6 . INVESTIGATORY ASSISTANCE TO FOREIGN SECURITIES AUTHORITIES.

(a) DEFINITION OF FOREIGN SECURITIES AUTHORITY. — Section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)) is amended by adding at the end thereof the following:

(50) The term "foreign securities authority" means any foreign government, or any governmental body or regulatory organization empowered by a foreign government to administer or enforce its laws as they relate to securities matters.

(b) AUTHORITY TO PROVIDE ASSISTANCE TO FOREIGN SECURITIES AUTHORITIES. — Section 21(a) of such Act (15 U.S.C. 78u(a)) is amended —

(1) by redesignating subsection (a) as subsection (a)(1); and

(2) by adding at the end thereof the following:

(2) On request from a foreign securities authority, the Commission may provide assistance in accordance with this paragraph if the requesting authority states that the requesting authority is conducting an investigation which it deems necessary to determine whether any person has violated, is violating, or is about to violate any laws or rules relating to securities matters that the requesting authority administers or enforces. The Commission may, in its discretion, conduct such investigation as the Commission deems necessary to collect information and evidence pertinent to the request for assistance. Such assistance may be provided without regard to whether the facts stated in the request would also constitute a violation of the laws of the United States. In deciding whether to provide such assistance, the Commission shall consider whether (A) the requesting authority has agreed to provide reciprocal assistance in securities matters to the Commission; and (B) compliance with the request would prejudice the public interest of the United States.

Section 7. SECURITIES LAWS STUDY.

(a) FINDINGS. — The Congress finds that —

(1) recent disclosures of securities fraud and insider trading have caused public concern about the adequacy of Federal securities laws, rules, and regulations;

(2) Federal securities laws, rules, and regulations have not undergone a comprehensive and exhaustive review since the advent of the modern international institutionalized securities market;

(3) since that review, the volume of securities transactions and the nature of the securities industry have changed dramatically; and

(4) there is an important national interest in maintaining fair and orderly securities trading, assuring the fairness of securities transactions and markets and protecting investors.

(b) STUDY AND INVESTIGATION REQUIRED . —

(1) GENERAL REQUIREMENT. — The Securities and Exchange Commission shall subject to the availability of funds appropriated pursuant to subsection (d) make a study and investigation of the adequacy of the Federal securities laws and

rules and regulations thereunder for the protection of the public interest and the interests of investors.

(2) REQUIRED SUBJECTS FOR STUDY AND INVESTIGATION. — Such study and investigation shall include an analysis of —

(A) the extent of improper trading while in possession of insider information, such as trading with advance knowledge of tender offers or forthcoming announcements of material financial information;

(B) the adequacy of surveillance methods and technologies of brokers, dealers, and self-regulatory organizations;

(C) the adequacy of cooperation between the Federal, State and foreign enforcement authorities concerning securities laws enforcement; and

(D) impediments to the fairness and orderliness of the securities markets and to improvements in the breadth and depth of the capital available to the securities markets, and additional methods to promote those objectives.

(3) CONDUCT OF STUDY AND INVESTIGATION. — In conducting the study and investigation required by this section, the Commission —

(A) may exercise any existing authority to gather information, including all power and authority the Commission would have if such investigation were being conducted pursuant to section 21 of the Securities Exchange Act of 1934;

(B) may consult with and obtain such assistance and information from other agencies in the executive and legislative branches of the Government (including the Department of Justice) as is necessary to enable the Commission to carry out this section;

(C) may appoint, without regard to the civil service laws, rules, and regulations, such personnel as the Commission deems advisable to carry out such study and investigation and to fix their respective rates of compensation without regard to such laws, rules, and regulations, but no such rate shall exceed the rate payable pursuant to section 5314 of title 5, United States Code; and

(D) may, on a reimbursable basis, use the services of personnel detailed to the Commission from any Federal agency.

(4) SUPPORT FROM OTHER AGENCIES —

(A) The head of any Federal agency —

(i) may detail employees to the Commission for the purposes of this section; and

(ii) shall provide to the Commission such information as it requires for the performance of its functions under this section, consistent with applicable law.

(B) The Comptroller General and the Director of the Office of Technology Assessment are authorized to assist the Commission in the performance of its functions under this section.

(c) REPORTS AND INFORMATION TO CONGRESS —

(1) GENERAL REPORT — The Commission shall report to the Congress on the results of its study and investigation within 18 months after the date funds to carry out this section are appropriated under subsection (d). Such report shall include the Commission's recommendations, including such recommendations for legislation as the Commission deems advisable.

(2) INTERIM INFORMATION TO CONGRESS . — The Commission shall keep the Committee on Energy and Commerce of the House of Representatives and the Committee on Banking, Housing, and Urban Affairs of the Senate, and the members thereof, fully informed on the progress of, and any impediments to completing, the study and investigation required by this section.

(d) AUTHORIZATION OF APPROPRIATIONS. — There are authorized to be appropriated $5,000,000 to carry out the study and investigation required by this section.

(e) DEFINITIONS — As used in this section —

(1) the term "Commission" means the Securities and Exchange Commission; and

(2) the term "Federal securities laws" has the meaning given the term securities laws by section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47)).

Section 8. COOPERATION WITH FOREIGN AUTHORITIES AND INTERNATIONAL ORGANIZATIONS IN ENFORCEMENT.

Section 35 of the Securities Exchange Act of 1934 is amended by adding at the end thereof the following new subsection:

(c) Funds appropriated pursuant to this section are authorized to be expended —

(1) for official reception and representation expenses, not to exceed $10,000 per year; and

(2) for the purpose of maintaining membership in and contributing to the operating expenses of the International Organization of Securities Commissions not to exceed $10,000 per year.

Section 9. EFFECTIVE DATE

The amendments made by this Act, except for section 6, shall not apply to any actions occurring before the date of enactment of this Act.