

MEMO# 11844

April 27, 2000

ICI COMMENT LETTER ON SEC PROPOSED SELECTIVE DISCLOSURE AND INSIDER TRADING RULES

1 See Memorandum to Closed-End Investment Company Committee No. 52-99 and SEC Rules Committee No. 113-99, dated December 29, 1999. 2 See Memorandum to Closed-End Investment Company Committee No. 9-00 and SEC Rules Committee No. 40-00, dated March 13, 2000. 1 [11844] April 27, 2000 TO: CLOSED-END INVESTMENT COMPANY COMMITTEE No. 15-00 SEC RULES COMMITTEE No. 66-00 RE: ICI COMMENT LETTER ON SEC PROPOSED SELECTIVE DISCLOSURE AND INSIDER TRADING RULES

The Institute today filed the attached comment letter on the SEC's proposed rules under the Securities Exchange Act of 1934 regarding selective disclosure and certain aspects of the law of insider trading. The Commission's proposal addresses three issues: (i) selective disclosure by issuers of material nonpublic information (Proposed Regulation FD (Fair Disclosure)); (ii) whether insider trading liability depends on a trader's "use" or "knowing possession" of material nonpublic information (Proposed Rule 10b5-1); and (iii) when the breach of a family or other non-business relationship may give rise to liability under the misappropriation theory of insider trading (Proposed Rule 10b5-2). 1 The comment letter, which is substantially similar to the draft letter previously circulated,² is briefly summarized below. The comment letter supports the objectives of the Commission's proposed new rules, which are to promote the full and fair disclosure of information by issuers, and to clarify and enhance existing prohibitions against insider trading. However, the letter expresses concern that the proposed rules could produce unintended marketplace consequences. The letter therefore recommends that the proposed rules be modified in certain respects to avoid such consequences while remaining consistent with the Commission's stated objectives. First, the letter recommends that, rather than using a standard relying on the amorphous concept of "materiality" to determine what information would be subject to disclosure under the rule, proposed Regulation FD be limited to those types of information that are especially likely to have a significant impact on the price of an issuer's securities (e.g., mergers and acquisitions, change in auditors, default on senior securities). The letter also urges the Commission to reaffirm the core principles of the "mosaic theory" as applicable to all research efforts conducted by analysts. Additionally, the letter recommends that closed-end investment companies not be subject to proposed Regulation FD. Second, the letter strongly recommends that, rather than adopting the "awareness" standard contained in proposed Rule 10b5-1, the Commission adopt a "use" test to determine when insider trading liability arises. The letter expresses concern that an awareness standard could inappropriately expose individuals to liability for activities that do not raise the concerns that the rule is designed to address. Additionally, the letter

supports adoption of subsection (c)(2) of proposed Rule 10b5-1, which recognizes the validity of a “Chinese Wall” defense. Finally, the letter recommends that the Commission expressly limit the application of proposed Rule 10b5-2 to the family and other personal relationships for which it is intended in order to avoid inadvertently inferring fiduciary-like relationships in other contexts involving confidentiality agreements. Doretha VanSlyke Zornada Assistant Counsel Attachment

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.