

**Statement for the Record by  
The U.S. Securities and Exchange Commission  
Before the  
House of Representatives Committee on Financial Services  
Subcommittee on Oversight and Investigations**

**July 13, 2009**

The Securities and Exchange Commission is pleased to have the opportunity to provide the Subcommittee with comments for the record in connection with the Subcommittee's hearing entitled, "Preventing Unfair Trading by Government Officials."

In light of the Commission's critical investor protection mission, we believe it is vital that all agency staff conduct themselves in accordance with the highest standards of ethical conduct in all matters concerning their personal financial holdings. The Commission's Office of the Inspector General recently issued a report in Case No. OIG-481 that identified weaknesses in the agency's compliance program. Even before that report was issued, the Commission had begun to take action to strengthen its oversight of employee securities transactions. The findings and recommendations in the report have reinforced the need for prompt action, and the Commission has responded in several ways. The steps taken by the Commission, outlined below, address and in some respects go beyond the Inspector General's recommendations.

The employees at the SEC have a well-deserved reputation for integrity and professionalism. When fully implemented, these measures will further bolster our standing by helping to prevent not only an actual impropriety, but the appearance of one as well. And these measures will ensure that the Commission's compliance program is second to none.

*Strengthened Rules:* We have proposed new rules governing trading by SEC employees.<sup>1</sup> The proposed new rules, which amend and expand the Commission's existing Rule 5, will:

- Require the pre-clearance of all trades.
- Prohibit all trading in the securities of a company under SEC investigation, regardless of whether the employee is aware of the investigation.
- Require all employees to authorize their brokers to provide duplicate trade confirmation statements to the agency.

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<sup>1</sup> In addition to the SEC's internal rules governing trading, SEC employees also have always been and will continue to be bound by generally applicable laws prohibiting the purchase or sale of securities based on material nonpublic information.

- Prohibit the ownership of securities in publicly-traded exchanges and transfer agents, in addition to existing prohibitions against owning securities in other firms directly regulated by the Commission.
- Require employees to certify that they do not have any non-public information about the company whose securities they are trading.
- Require supervisors to conduct periodic reviews of employee securities transactions and compare any transactions to the employee's work projects.

These rules were submitted to the Office of Government Ethics ("OGE") on May 22, 2009, and we are in the process of working with OGE to finalize them.

*Modernized Computer Compliance System:* We recently contracted with an outside firm specializing in automated compliance systems to develop a new computer compliance system for the agency. This modernized system will automate and simplify the transaction reporting process and make it easier to verify and monitor employee trading. We expect the new system to be operational within three months. Six months after the computer system is in place, we will bring on board a compliance expert to review the system and ensure the program is operating effectively.

*New Chief Compliance Officer Position:* We have created a new Chief Compliance Officer position to oversee the agency's compliance program. The position was posted on May 18, 2009. We have already received applications from a number of candidates for the position and begun the interview process.

*Organizational Changes:* The Chairman recently consolidated responsibility for the oversight of employee securities transactions within the SEC's Ethics Office and directed that additional staff resources be devoted to monitoring, reviewing, and spot-checking these transactions.

In its March 3, 2009 report, the SEC's Office of the Inspector General made eleven recommendations concerning the agency's compliance program. As we have advised the Inspector General, the steps outlined above and other actions by the Commission address each of these recommendations:<sup>2</sup>

1. Consolidation of responsibility for ensuring compliance with Rule 5 in one office: As discussed above, the Commission has consolidated responsibility for securities transaction monitoring and review in the Ethics Office.

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<sup>2</sup> In addition to these eleven recommendations concerning Commission policies and practices, the Inspector General also recommended disciplinary action against two employees identified in the report. As we have advised the Inspector General, we have deferred consideration of an appropriate response to this recommendation based on what we understand to be a pending criminal inquiry by the U.S. Attorney's Office. Such a deferral ensures that any disciplinary action is consistent with the results of the U.S. Attorney's Office's review and eliminates the risk that Commission action would interfere with any criminal inquiry or be viewed as prejudging whether any criminal violation occurred. At the appropriate time, we will consider what, if any, disciplinary action should be taken.

2. Integrated computer compliance system: We have already retained an outside firm to build this system.
3. Requiring duplicate brokerage confirmations: The proposed new securities trading rules will require employees to authorize their brokers to supply the Commission with duplicate trade confirmations.
4. Requiring certification that employee does not possess non-public information: When the new compliance system is in place, employees making a trade will certify as part of the pre-clearance process that they do not possess any nonpublic information about the company whose securities they are trading. In the interim, we have amended Form 681, the employee securities transaction reporting form, to require such a certification.
5. Review of transaction reporting forms to ensure that clearance was obtained and trade was timely made: The new computer compliance system will ensure that pre-clearance is obtained and will enable the monitoring of subsequent trading activity.
6. Supervisory review of employee securities holdings: The new rules will require periodic supervisory review of employee securities transactions and comparison to the employee's work projects for any conflicts, apparent or real.
7. Spot-checks for compliance with trading rules: Once the new system and rules are in place, we will monitor all employees' compliance with trading rules on a real-time basis. This response goes beyond the recommended action.
8. Expanded training: We will conduct a thorough training program on the new rules and computer compliance system once they are in place, and we expect that this training will be consonant with this recommendation. In addition, since the Inspector General issued its report, the Chairman and the Ethics Office have both issued guidance to agency staff concerning duties with respect to securities trading.
9. Comparison of securities holding and securities transaction reporting forms to ensure accuracy: Again, once the new system and rules are in place, all employee securities transactions will be monitored on a real-time basis. This response goes beyond the recommended action.
10. Expansion of duty to file Form 450 (financial disclosure form): The new rule, coupled with the computer compliance system, will address this concern about the scope of the obligation to file financial disclosure forms by ensuring that securities transactions by all employees are recorded and monitored.

11. Written policy concerning confidentiality of SEC information: Our Office of General Counsel will be working with the Division of Enforcement to review our policies concerning confidential information and ensure that such information is safeguarded appropriately. In addition, the new requirements that all securities trades be pre-cleared, that no employee may trade in the securities of any company under investigation, and that every employee making a trade must certify that he or she does not possess any nonpublic information about the company at issue will address the risk of employee trading based on non-public information.

Thank you for the opportunity to submit this statement for the record. We hope that our comments will be useful to the Subcommittee.