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Prying Open Swiss Vaults: The SEC's Investigation of Insider Trading in the Santa Fe Case

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PRYING OPEN SWISS VAULTS: THE SEC'S
INVESTIGATION OF INSIDER TRADING IN THE
SANTA FE CASE

H.L. Silets*

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INTRODUCTION

In recent years, the United States Securities and Exchange Commission (SEC)¹ has increased its efforts to combat insider trading² by indi-

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1. The United States Congress enacted the Securities Exchange Act of 1934, Pub. L. No. 291, 48 Stat. 881 (1934) (codified as amended at 15 U.S.C. §§ 78a-78hh (1982)). Through the 1934 Act, Congress established the SEC. *Id.* at § 78d. The SEC is an independent, nonpartisan agency of the United States government with primary responsibility for administering and enforcing securities laws. It requires disclosure of the structure of all public companies and registration of all securities exchanged. The SEC consists of five members appointed for staggered five year terms. It hears complaints, initiates investigations, issues brokerage licenses, and has broad powers to penalize fraud. It is also a policy-making body, with a staff of over two thousand. SECURITIES AND EXCHANGE COMMISSION, *THE WORK OF THE SECURITIES AND EXCHANGE COMMISSION*, reprinted in W. CARY & M. EISENBERG, CORPORATIONS A-67 (5th ed. 1980).

2. *Memorandum of the Securities and Exchange Commission in Support of the*

viduals who attempt to shield their illegal profits behind Switzerland's traditional veil of bank secrecy.³ Swiss laws that prohibit the disclosure of the bank customers' identities, except in certain limited circumstances, have frustrated the SEC's ability to identify individuals trad-

Insider Trading Sanction Act of 1982, 14 SEC. REG. & L. REP. (BNA) No. 38, at 1705 n.1 (Oct. 1, 1982) [hereinafter cited as SEC Memo]; SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969). Insider trading is the term used to describe the purchase and sale of securities based on material information not available to the public. "Insider traders" or "insiders" may be broadly defined to include anyone who has "access, directly or indirectly, to information intended to be available only for a corporate purpose and not for the personal benefit of anyone." In the Matter of Cady, Roberts & Co., 40 S.E.C. 907, 912 (1961). Insider trading is illegal under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1982) and Rule 10b-5, 17 C.F.R. § 240.10b-5 (1985), promulgated by the SEC to deal with the regulation and use of manipulative devices. These are general provisions prohibiting fraud in connection with the purchase or sale of a security. Willful violations of the Securities Exchange Act or rules promulgated thereunder are criminal under § 32 of the Act, 15 U.S.C. § 78ff(a) (1982), and carry a potential penalty of a \$10,000 fine or five years in prison or both. *Id.* In addition, individuals may be liable for trading on the basis on nonpublic information concerning pending tender offers. Rule 14e-3, 17 C.F.R. § 240.14e-3 (1985). The SEC cannot bring criminal actions itself, but it may "transmit such evidence as may be available concerning such acts or practices as may constitute a violation . . . to the Attorney General." 15 U.S.C. § 78u(d) (1982). The Attorney General then has the usual prosecutorial discretion in deciding whether to institute criminal proceedings. 15 U.S.C. § 78ff (1982). See generally Hazen, *Corporate Insider Trading: Reawakening the Common Law*, 39 WASH. & LEE L. REV. 845 (1982) (analyzing insider trading problems); Brudney, *Insiders, Outsiders, and Informational Advantages under the Federal Securities Laws*, 93 HARV. L. REV. 322 (1979) (same); Deitz, *A Practical Look at Section 16(b) of the Securities Exchange Act*, 43 FORDHAM L. REV. 1 (1974) (same); Note, *SEC Rule 10b-5: A Recent Profile*, 13 WM. & MARY L. REV. 860 (1972) (same); Manne, *In Defense of Insider Trading*, 44 HARV. BUS. REV. 113 (Nov.-Dec. 1966) (same).

3. Swiss Federal Act on Banks and Savings Banks of November 8, 1934, art. 47 (*as amended*). This article states:

1. Whoever discloses a secrecy that has been entrusted to him or which he has received knowledge in his capacity as official, employee, agent, liquidator or commissioner of a bank, as observer of the banking commission, as official or employee of a recognized auditing firm, or whosoever attempts to induce somebody else to commit such a violation of professional secrecy shall be punished with imprisonment up to six months or with a fine up to 50,000 francs.
2. If the act has been committed by negligence, the penalty shall be a fine up to 30,000 francs.
3. The violation of professional secrecy remains punishable beyond the termination of the official or professional relationship, or the exercise of the profession.
4. Excepted are Federal and cantonal provisions concerning the duty to testify and the duty to present information to an official.

Amtliche Sammlung der Bundesgesetze und Verordnungen [AS] (Official Collection of Federal Laws and Regulations) 1971, at 808 (translation by Meier, *Banking Secrecy and International Taxation*, 7 INT'L LAW. 16, 18 (1973)) [hereinafter cited as Article 47]. The law applies to all Swiss banks and Swiss branches of foreign banks. Mueller, *The Swiss Banking Secret From a Legal View*, 18 INT'L & COMP. L.Q. 360, 363 (1969).

ing on inside information through Swiss banks.⁴ The customers of Swiss banks avoid prosecution for insider trading because records for such transactions merely reveal trading for the benefit of the bank.⁵ Given the high volume of securities that Swiss banks trade in the United States,⁶ the SEC has recognized and responded to the growing need to eliminate the deleterious practice⁷ of insider trading.⁸

4. Most major Swiss banks are able to buy and sell securities through "omnibus accounts" with brokerage houses in the United States. Unlike banks in the United States, Swiss banks are allowed to engage in retail stock brokerage activities in addition to conventional commercial banking operations. Meyer, *Swiss Banking Secrecy and Its Legal Implications in the United States*, 14 NEW ENG. L. REV. 18, 45 (1978). Swiss banks often act as agents in investing the deposits of customers who want to trade securities on a United States exchange. When a bank purchases and sells securities, it places an order with a brokerage house in the bank's name and posts the transaction to the customer's secret account. Consequently, the broker never discovers the identity of the bank's customer for whom the transaction was made. See *Foreign Bank Secrecy and Bank Records: Hearings on H.R. 15073 Before the House Comm. on Banking and Currency*, 91st Cong., 1st and 2nd Sess. 20 (1969-70) [hereinafter cited as 1969-70 Hearings] (statement of Robert N. Morgenthau, U.S. Attorney for the Southern District of New York).

5. *Hearings on S. 3678 and H.R. 15073 Before the Subcomm. on Financial Institutions of the Senate Comm. on Banking and Currency*, 91st Cong., 2d Sess. 58 (1970) [hereinafter cited as 1970 Hearings] (statement of Will Wilson, Assistant Attorney General). Because of Switzerland's strict bank secrecy laws, Swiss bank accounts allegedly have been used to conceal income, commit fraudulent tax maneuvers, violate SEC margin requirements, and circumvent other securities regulations. See generally 1969-70 Hearings, *supra* note 4 (describing the use of Swiss bank accounts to evade U.S. securities laws and regulations).

6. In 1981, roughly \$14.8 billion (approximately twenty percent) of the total foreign trading on American stock exchanges came from Swiss banks. N.Y. Times, Sept. 1, 1982, at D13, col. 6.

7. In enacting the Securities Exchange Act of 1934, *supra* note 1, Congress sought to ensure the integrity of the market in order to establish public confidence and encourage open trading. See S. REP. NO. 47, 73d Cong., 1st Sess. 1 (1933) (discussing the specific goals of the Securities and Exchange Act of 1934). The Securities Exchange Act addressed the problem of insider trading in particular. The Senate Banking and Currency Committee stated in a 1934 report that:

Among the most vicious practices unearthed at the hearings before the subcommittee was the flagrant betrayal of their fiduciary duties by directors and officers of corporations who used their positions of trust and the confidential information which came to them in such positions, to aid them in their market activities.

S. REP. NO. 1455, 73d Cong., 2d Sess. 55 (1934). Congress, therefore, declared insider trading illegal because the practice undermines the expectation of fairness in securities markets. SEC Memo, *supra* note 2, at 1706; see also *Chiarella v. United States*, 445 U.S. 222 (1980) (prohibiting insider trading); Cary, *Insider Trading in Stocks*, 21 BUS. LAW. 1009, 1010 (1966) (discussing problem of insider trading in stocks).

8. The SEC has stepped up its efforts to combat insider trading within recent years. From 1966 to 1980, there were only thirty-seven reported actions based on thirty-five separate incidents of insider trading. Dooley, *Enforcement of Insider Trading Restrictions*, 66 VA. L. REV. 1, 8-9 (1980). Prior to 1978, the SEC initiated about forty cases involving insider trading. From 1978 to the present, over fifty insider trading cases have been brought, twenty of them since July 1981. *Extensions of Remarks, Insider Trading Sanctions Act of 1982*, H.R. 7352, 97th Cong., 2d Sess., 128 CONG. REC. E4996

In its attempt to combat insider trading, the SEC's Division of Enforcement constantly observes the trading activities of securities exchanges throughout the United States.⁹ During the trading day, information-retrieval devices and computers monitor the securities markets and signal unusual trading volumes or major price fluctuations.¹⁰ When questionable circumstances regarding a market transaction indicate that securities laws may have been violated, the SEC begins investigating the source of the trading activity by evaluating buy and sell orders.¹¹ Following a preliminary SEC investigation,¹² a formal investigation may ensue.¹³

One of the most important insider trading cases brought by the SEC to date involves the events surrounding the 1981 takeover of the Santa Fe International Corporation by the Kuwait Petroleum Corporation.¹⁴ The resultant action (the *Santa Fe* case) has led to two monumental decisions¹⁵ by the Swiss Federal Tribunal;¹⁶ the involuntary return of illegal profits by certain inside traders,¹⁷ and the signing of the Memorandum of Understanding on Insider Trading (MOU)¹⁸ by the United

(daily ed. Dec. 8, 1982) (statement of Rep. Benjamin Rosenthal).

9. Note, *Insider Trading Laws and Swiss Banks: Recent Hope for Reconciliation*, 22 COLUM. J. TRANSNAT'L L. 303, 305 (1984).

10. Louis, *The Unwinnable War on Insider Trading*, FORTUNE, July 13, 1981, at 72, 76.

11. *Id.* at 76.

12. Enforcement Activities, 17 C.F.R. § 202.5(a) (1985) (describing the investigative and enforcement mechanisms available to the SEC).

13. *Id.* (specifically permitting the SEC to institute formal investigations).

14. Securities and Exchange Comm'n v. Certain Unknown Purchasers of the Common Stock and Call Options for the Common Stock of Santa Fe Int'l Corp. (1981-82 Transfer Binder) FED. SEC. L. REP. (CCH) ¶ 98,323 (S.D.N.Y. Oct. 26, 1981) (No. 81 Civ. 6553) [hereinafter cited as *SEC v. Certain Unknown Purchasers*].

15. *Switzerland: Swiss Supreme Court Opinion In The Second Santa Fe Case Concerning Judicial Assistance*, 24 I.L.M. 745 (May 1985) [hereinafter cited as *Second Swiss Opinion*] (English translation prepared by Charles Poncet of Lalive & Budin, Geneva); *Switzerland: Swiss Supreme Court Opinion Concerning Judicial Assistance in the Santa Fe Case*, 22 I.L.M. 785 (July 1983) [hereinafter cited as *First Swiss Opinion*] (reproduced from an English summary prepared by Charles Poncet of Lalive & Budin, Geneva).

16. *Second Swiss Opinion*, *supra* note 15, at 746 n.3; Béguin, *Insider Trading in Switzerland After Santa Fe*, INT'L FIN. L. REV., Nov. 1983, at 10. The Swiss Federal Tribunal is the Supreme Court of Switzerland.

17. See N.Y. Times, Feb. 27, 1986, at 33, col. 1 (citing examples of seven individuals who settled their cases with the SEC for approximately \$7.8 million). An eighth person, a director of Santa Fe International, settled SEC charges against him in September 1982 by agreeing to pay over \$300,000 in profits made illegally through insider trading. Wall St. J., Sept. 30, 1982, at 8, col. 3. See *infra* notes 200-05 and accompanying text (discussing the deterrent effect of the return of illegal profits).

18. Memorandum of Understanding to Establish Mutually Acceptable Means for Improving International Law Enforcement Cooperation in the Field of Insider Trading, Aug. 31, 1982, United States-Switzerland, 22 I.L.M. 1 (1983), *reprinted in* 14 SEC.

States and Switzerland in 1982. Indeed, the *Santa Fe* case represents one of the largest and most significant insider trading probes ever conducted by the SEC.¹⁹

This Note will examine the SEC's efforts to extract information from the Swiss government concerning the unknown inside traders in the *Santa Fe* case. In particular, it will consider the SEC's attempts to obtain judicial assistance from Swiss authorities based on both the Treaty on Mutual Assistance in Criminal Matters (Mutual Assistance Treaty) between the United States and Switzerland²⁰ and the subsequent Memorandum of Understanding (MOU). This Note also will discuss the two decisions rendered in this case by the Swiss Federal Tribunal and their effect upon the *Santa Fe* litigation.

REG. & L. REP. (BNA) No. 39 at 1737-42 (Oct. 8, 1982) [hereinafter cited as Memorandum of Understanding]. A memorandum of understanding is not a binding agreement subject to ratification by the United States Senate or the Swiss Parliament, but rather, is an expression of intent by the two governments. SEC Press Release No. 82-44 (Sept. 1, 1982) [hereinafter cited as SEC Release].

19. Wall St. J., June 10, 1983, at 12, col. 3. After bringing the *Santa Fe* case, Congress criticized the SEC for focusing too much attention on insider trading investigations at the expense of its other enforcement responsibilities. *SEC is Criticized for Decision Not to Bring Action Against Citicorp*, 14 SEC. REG. & L. REP. (BNA) No. 36, at 1564, 1565 (Sept. 17, 1982) (reporting the comments of Rep. John Dingell in Hearing Before the Oversight and Investigations Subcommittee of the House Energy and Commerce Committee). Insider trading cases constituted twenty of the two hundred fifty-two enforcement cases which the SEC initiated during the fiscal year ending September 30, 1982. *SEC's Shad, Fedders Deny Commission Overemphasizing Insider Trading*, 14 SEC. REG. & L. REP. (BNA) No. 41, at 1785 (Oct. 22, 1982); see also *supra* note 8 and accompanying text (describing the SEC's recent efforts against insider trading).

The cooperation resulting from the United States and Swiss agreement in the *Santa Fe* case laid the foundation of cooperation for cases to follow. On May 12, 1986, Dennis Levine, a Wall Street merger specialist, was charged with insider trading which reaped \$12.6 million dollars over a period of five years. N.Y. Times, May 13, 1986, at 1, col. 3. In the largest insider trading action ever brought by the SEC, the full cooperation of the Swiss bank from which Levine conducted his trades provided bank records that identified Levine's involvement in trading at the Swiss bank's subsidiary in the Bahamas. N.Y. Times, May 15, 1986, at 27, col. 3. The action by the Swiss bank represents the increasing recognition by the Swiss of insider trading as a violation that secrecy laws will not protect—a type of protection for which Switzerland and the Bahamas are noted.

It was not clear whether Bank Leu, the Swiss parent of the Bahamas subsidiary, acted independently or by the direction of the Swiss government. *Id.* According to the 1982 MOU, the SEC could have gained access to the bank records through a lengthy legal process in which the SEC would have to prove that the bank client violated both Swiss and U.S. law. In this case, however, a spokesman for Bank Leu stated that, despite the principle of confidentiality, insider trading actions of this type "have no place in our bank." *Id.*

20. Treaty Between the United States of America and the Swiss Confederation on Mutual Assistance in Criminal Matters, May 25, 1973, United States-Switzerland, 27 U.S.T. 2021, T.I.A.S. No. 8302 (effective date Jan. 23, 1977) [hereinafter cited as Mutual Assistance Treaty].

I. THE MUTUAL ASSISTANCE TREATY AND THE MEMORANDUM OF UNDERSTANDING

Switzerland's strict banking secrecy laws prohibiting the disclosure of any financial information relating to a customer's bank account seriously frustrate SEC investigations. Article 47 of the Swiss Penal Code²¹ provides that an individual may be fined or imprisoned for disclosing bank secrets without a prior waiver by the bank's customer²² of authorization by a government official.²³ Moreover, Penal Code Article 273 prohibits disclosure of any "business secret" to another business or to a "foreign official agency."²⁴ Thus, by preventing banks from disclosing the identities of customers for whom the banks effect securities transactions to the SEC, insiders "trade securities in the American markets without fear of identification."²⁵ Even in cases where the SEC has identified alleged improprieties or illegalities, Swiss secrecy provisions have blocked attempts by the SEC to enforce federal securities laws.²⁶ In addition, the traditional reluctance of United States courts to order United States citizens residing or doing business abroad to comply with federal subpoenas often in violation of foreign laws has further undermined the SEC's effectiveness.²⁷

21. Article 47, *supra* note 3.

22. Meyer, *The Banking Secret and Economic Espionage in Switzerland*, 23 GEO. WASH. L. REV. 284, 293 (1955).

23. See Article 47, para. 4, *supra* note 3 (stating the exception to the Swiss bank secrecy provision).

24. Article 273 states:

A person who, through searching, secures a manufacturing or business secret, in order to make it accessible to a foreign official agency, or to a foreign organization, or to a private business enterprise, or to their agents, a person who makes accessible a manufacturing or business secret to a foreign official agency, or to a foreign organization, or to a private business enterprise, or to their agents, shall be punished by imprisonment, in serious cases in the penitentiary. In addition a fine may be imposed.

Schweizerisches Strafgesetzbuch [StGB] art. 273, Code pénal suisse [Cp] art. 273; Codice penale svizzero [Cp.] art. 273 (translation by Meyer, *supra* note 22, at 302) (this article not having changed despite other revisions and amendments to the Swiss Penal Code in 1971).

25. B. Thomas, Remarks at the Meeting of the Association of the Bar of the City of New York 5, 8 (Oct. 4, 1982).

26. See generally Panel on Disclosure and Enforcement Problems, SEC Conference on Major Issues Confronting the Nation's Financial Institutions and Markets in the 1980's, Executive Summary 4-5, Oct. 6-8, 1982 [hereinafter cited as Major Issues Conference] (referring to secrecy provisions throughout the international banking system rather than just specifically to Swiss secrecy provisions); Note, *The Effect of the U.S.-Swiss Agreement on Swiss Banking Secrecy and Insider Trading*, 15 L. & POL'Y INT'L BUS. 565, 566-67 n.8 (1983) (same).

27. Note, *Foreign Bank Secrecy and the Evasion of United States Securities Laws*, 9 N.Y.U.J. INT'L L. & POL'Y 417, 418 (1977).

Although Congress first prohibited insider trading in 1934,²⁸ the SEC has only pursued inside traders vigorously since 1979.²⁹ Growing international participation in United States securities exchanges,³⁰ the increasing volume of securities trading, and the internationalization of businesses have expanded the opportunities for traders to capitalize on inside information.³¹ Furthermore, insider trading has become an extremely profitable and low-risk practice due to the sudden increase in the number of corporate mergers, tender offers and acquisitions, and the traditional leniency of SEC enforcement.³²

A. PROBLEMS WITH AND GOALS OF THE MUTUAL ASSISTANCE TREATY

After five years of negotiations, representatives of the United States and Switzerland signed the Mutual Assistance Treaty on May 25, 1973.³³ The Mutual Assistance Treaty, which went into effect on January 23, 1977, provides for "mutual assistance in investigations or court proceedings" involving criminal offenses.³⁴ Because of the intricate banking laws involved in the negotiations and the fact that it was the first treaty of mutual assistance in criminal matters negotiated by the U.S., it is the longest and most complicated of any mutual assistance treaty signed by the United States.³⁵

The drafters of the Mutual Assistance Treaty attempted to pierce the stringent Swiss bank secrecy provisions by providing for disclosure of Swiss banking information to United States regulatory agencies upon formal requests in certain circumstances.³⁶ In general, the Treaty

28. See Securities and Exchange Act of 1934, *supra* notes 1 and 7 (describing the SEC's functions in both broad terms and with particular reference to insider trading).

29. See *supra* note 8 (describing the SEC's efforts to bring insider trading cases). See generally Wall St. J., Dec. 18, 1981, at 22, col. 2 (discussing the SEC's goal of curbing the abuses of secret corporate information).

30. Major Issues Conference, *supra* note 26, at 2-5. Between 1971 and 1981, foreign financial institutions increased their level of activity in United States securities markets from \$71 billion to \$198 billion. Moreover, total foreign investment increased from \$25.6 billion to \$74.6 billion. *Id.* See also N.Y. Times, Sept. 1, 1982, at D13, col. 6 (discussing increasing foreign investment).

31. Major Issues Conference, *supra* note 26, at 2-5.

32. *Id.* at 4-5. See also *supra* note 8 (describing the SEC's efforts to combat insider trading in recent years).

33. Mutual Assistance Treaty, *supra* note 20; Note, *The Recent Swiss-American Treaty to Render Mutual Assistance in Criminal Law Enforcement (An Application of the Bank Secrecy Act): Panacea or Placebo?*, 7 N.Y.U.J. INT'L POL'Y 103 (1974).

34. Mutual Assistance Treaty, *supra* note 20, at art. 1, para. 1(a).

35. Ellis & Pisani, *The United States Treaties on Mutual Assistance in Criminal Matters: A Comparative Analysis*, 19 INT'L LAW. 189, 197-98 (1985).

36. Memorandum of Understanding, *supra* note 18, at art. II, paras. 1, 2; Mutual Assistance Treaty, *supra* note 20, at art. 1. While the Mutual Assistance Treaty pro-

provides a broad range of assistance in criminal matters including: (1) executing requests relating to criminal matters; (2) obtaining statements or testimony; (3) producing and authenticating documents, records, or articles of evidence; (4) returning to the requesting party any articles, objects or any other property or assets illegally obtained by the accused or rightfully belonging to the requesting party; (5) serving judicial documents, summonses, writs, records of court judgments of decisions and judicial verdicts; (6) producing an expert or a witness before a court of the requesting party; (7) locating witnesses; and (8) furnishing evidence and judicial records.³⁷

"Compulsory assistance" measures included in the Treaty allow a requesting State to obtain information from the requested State when a crime is committed within the requested State's jurisdiction.³⁸ A requesting State may use these compulsory assistance measures when: (1) the offense is criminally punishable under the laws of the requested State if committed within its jurisdiction; (2) the offense is included in the Treaty's Schedule of Offenses;³⁹ (3) the offense constitutes unlawful bookmaking, lottery, or gambling;⁴⁰ or (4) the offender is involved in an organized crime group.⁴¹ In addition, compulsory assistance is available only when the offense under investigation is a crime in both the United States and Switzerland.⁴²

Insider trading is not a crime under the Swiss Penal Code⁴³ and it is

vides for assistance in *any* criminal matter, the MOU assists in criminal actions involving the banking system and especially securities violations.

37. Mutual Assistance Treaty, *supra* note 20, at art. 1, paras. 4, 11, 16, 19, 20, 22. See Ellis & Pisani, *supra* note 35, at 198 (detailing some aspects of the assistance furnished in criminal matters).

38. Mutual Assistance Treaty, *supra* note 20, at art. 4, para. 1 (providing that the requesting state shall employ only those compulsory measures available in the requested state for offenses committed within its jurisdiction).

39. Mutual Assistance Treaty, *supra* note 20, at art. 4, para. 2(a) (referring to Schedule of Offenses). The Mutual Assistance Treaty contains a Schedule of Offenses listing thirty-five violations that constitute crimes in both countries and that require resolution through the mutual assistance of both parties. The Schedule lists counterfeiting, forgery, drug violations, gambling and bookmaking operations, fraud in business dealings, conspiracy to commit such offenses, and other crimes such as murder, theft, and rape. Seven exchanges of letters that supplement the Treaty interpret language used in several of the Articles dealing with limits on the use of information, the duty to testify in the requested state, testimony to authenticate documents, the protection of secrecy, the taking of oaths, and the service of documents. Ellis & Pisani, *supra*, note 35, at 198 n.50. See generally M. NASH, DIGEST OF UNITED STATES PRACTICE IN INTERNATIONAL LAW 859-65 (1978) (suggesting a model mutual assistance treaty).

40. Mutual Assistance Treaty, *supra* note 20, at art. 4, para. 2(b).

41. *Id.* at art. 6, para. 2(a) (referring to the general requirements for the application of the special provisions concerning organized crime).

42. *Id.* at art. 4, para. 2(a).

43. See Memorandum of Understanding, *supra* note 18, at art. 1, para. 2 (stating

not included in the Schedule of Offenses under which assistance definitely is available under the Treaty.⁴⁴ Although fraud is included in the Schedule of Offenses, it is unclear from the Treaty itself whether securities law violations are included under the general category of fraud.⁴⁵ Under the Treaty, it is also unclear whether the Swiss Federal Office for Police Matters⁴⁶ necessarily would assist investigations by United States officials of Swiss criminal offenses not covered by the Schedule of Offenses.⁴⁷

The Treaty, therefore, does not guarantee the disclosure of Swiss banking information. For example, the Treaty grants officials of the requested State the right to refuse investigative assistance to the requesting State if obliging the request for information would "prejudice sovereignty, security, or similar essential interests."⁴⁸ Additional difficulties arise when the requesting State requires investigative assistance regarding an offense punishable in the requested State but not listed in the Schedule of Offenses.⁴⁹ Furthermore, the Treaty lists a number of offenses for which requests for assistance "shall not apply." These include extradition requests, execution of judgments in criminal matters,

that while insider trading is not *per se* punishable in Switzerland, it is considered dishonorable); ARNOLD, SWITZERLAND IN COMPARATIVE SURVEY OF SECURITIES LAWS: A REVIEW OF THE SECURITIES AND RELATED LAWS OF FOURTEEN NATIONS 176 (J. Robinson ed. 1980) (same); Jenckel & Rider, *The Swiss Approach to Insider Dealing*, 128 NEW L.J. 683, 683 (1978) (same). *But see* Wall St. J., Oct. 8, 1986, at 39, col. 1 (reporting that the Swiss Senate overwhelmingly approved a bill outlawing insider trading and that the Swiss lower house is expected to approve the bill in the near future). The proposed law would punish insider traders with both imprisonment and fines. If the legislation passes in the lower house, it could be in effect by January 1988.

44. Mutual Assistance Treaty, *supra* note 20 at art. 4, para. 2(a) (referring to the Schedule of Offenses for which compulsory measures are available).

45. *See id.* at art. 4, para. 2(a) (referring to the Schedule of Offenses, in particular item 19). It is unclear whether securities law violations should be considered fraud under the Treaty because such violations are not recognized as fraudulent acts under Swiss law. In addition, the Treaty may be used to overcome Swiss secrecy laws only where the offense involved is criminal under the laws of both the United States and Switzerland; *see supra* notes 36-38 and accompanying text.

46. The Swiss Federal Office for Police Matters, which is equivalent to the FBI in the United States, is Switzerland's government law enforcement agency. *See* Comment, *The Effect of Swiss Bank Secrecy on the Enforcement of Insider Trading Regulations and the Memorandum of Understanding Between the United States and Switzerland*, 7 B.C. INT'L COMP. L. REV. 541, 563 n.212 (1984) (based on a telephone conversation the author of the comment had with a member of the SEC Enforcement Division).

47. Greene, *U.S., Switzerland Agree to Prosecute Insider Traders*, Legal Times of Washington, Oct. 4, 1982, at 14, col. 1.

48. Mutual Assistance Treaty, *supra* note 20, at art. 3, para. 1(a). Prior to refusal of the request, the requested State must examine alternative plans to satisfy the request. *Id.* at art. 3, para. 2. If the requested State can design an alternate plan, then assistance may be rendered under that method. *Id.*

49. *Id.* at art. 4, para. 3.

investigations concerning political and military offenses, and "violations with respect to taxes, custom duties, governmental monopoly charges or exchange control regulations," except as they may relate to certain offenses listed in the Schedule.⁵⁰ In addition, the Treaty does apply to cases involving antitrust or fiscal and political matters.⁵¹ Finally, a requesting State may be denied information that relates to the prosecution of a person for acts that have led to his conviction or acquittal for a substantially similar offense by a final judgment of a court in the requested State.⁵²

The Mutual Assistance Treaty does not discuss specifically the issue of Swiss banking secrecy.⁵³ In Treaty correspondence interpreting article 3(1), however, the United States and Switzerland recognized that disclosing banking information might prejudice the "similar essential interests" of the requested State.⁵⁴ The parties agreed, therefore, that the requested State may refuse the requesting State's appeal for investigative assistance only if the assistance would breach the banker-client confidentiality privilege.⁵⁵

The SEC has experienced difficulty in implementing the Mutual Assistance Treaty during its investigations of suspected insider trading.⁵⁶ Indeed, the SEC has never successfully implemented the Treaty in the prosecution of an insider trading case.⁵⁷ This is perhaps because, until recently, it was uncertain whether the Treaty mandated the disclosure

50. *Id.* at art. 2, para. 1.

51. *Id.* at art. 2, para. 2; *see also supra* note 41 and accompanying text (referring to the general requirements for applying the special provisions on organized crime).

52. Mutual Assistance Treaty, *supra* note 20, at art. 3, para. 1(b).

53. Meyer, *supra* note 4, at 65.

54. Mutual Assistance Treaty, *supra* note 20, Interpretative Letters from Sheldon Cullen Davis, United States Ambassador to Switzerland, to Dr. Albert Weitnauer, Ambassador of Switzerland to the United States, on May 25, 1973. The Letter of May 25, 1973, stated:

It is the understanding of the United States Government that Swiss bank secrecy and Article 273 of the Swiss Penal Code shall not serve to limit the assistance provided for by this Treaty, except as provided by paragraph 2 of Article 10.

It is nevertheless understood that the disclosure of facts which a bank is ordinarily required to keep secret could in exceptional circumstances also constitute facts the transmission of which to the requesting State would be likely to result in prejudice to the "similar essential interests" of the requested State. Similarly, the disclosure of facts which are manufacturing or business secrets could in exceptional circumstances be of such significant importance that it would result in prejudice to "similar essential interests" of the requested State. In either case, the requested state would have the right, under paragraph 1 of Article 3, to refuse assistance.

55. *Id.*; *see also* Memorandum of Understanding, *supra* note 18.

56. *See* Note, *supra* note 26, at 587.

57. *See* Comment, *supra* note 46, at 563 n.214.

of confidential Swiss banking information in cases where investors used Swiss banks to hide violations of United States securities laws.⁵⁸ Although trading on the basis of material,⁵⁹ nonpublic,⁶⁰ information constitutes fraud in the United States, Swiss penal law contains no readily identifiable equivalent.⁶¹ Thus, banks that reveal such information remain potentially liable under either article 273 of the Swiss Penal Code⁶² or article 47(b) of the Public Banking Law.⁶³

Another problem in applying the Mutual Assistance Treaty to insider trading is that while the terms of the Treaty apply solely to criminal law enforcement⁶⁴, the SEC initiates only civil suits against inside traders.⁶⁵ Under United States law, the United States Department of Justice has exclusive authority to initiate criminal proceedings against inside traders.⁶⁶ Therefore, to circumvent Switzerland's traditional veil of bank secrecy, the SEC has attempted to apply the Schedule of Offenses to invoke the compulsory assistance provisions of the Treaty.⁶⁷

58. On January 26, 1983, the Swiss Federal Tribunal decided that the Treaty did not require the disclosure of confidential Swiss banking information to United States authorities investigating alleged violations of United States insider trading laws. See *First Swiss Opinion*, *supra* note 15; see also *infra* notes 141-68 and accompanying text.

59. Information is material if a substantial likelihood exists that a reasonable stockholder would consider that information important in making investment decisions. *TSC Industries v. Northway*, 426 U.S. 438, 449 (1976). Although *Northway* did not involve allegations of insider trading, courts have used this materiality standard in such cases. *Joyce v. Joyce Beverages*, 571 F.2d 703, 707 n.6 (2d Cir. 1978), *cert. denied*, 437 U.S. 905 (1978).

60. Nonpublic information is that which is not generally known in the marketplace. See *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833 (2d Cir. 1968) (en banc), *cert. denied*, 394 U.S. 976 (1969) (significance of a mineral discovery known only to a few corporate employees and officers).

61. Greene, *supra* note 47, at 12, col. 4.

62. See *supra* note 24 and accompanying text (translating text of Swiss Penal Code at 273).

63. See *supra* note 3 and accompanying text (citing translation of text of Art. 47 of the Swiss Federal Act on Banks and Savings Banks of Nov. 8, 1934, as amended).

64. Mutual Assistance Treaty, *supra* note 20.

65. 15 U.S.C. § 78u(d) (1982). The SEC refers insider trading cases to the Department of Justice for criminal prosecution. See *supra* note 2 and accompanying text; see also Greene, *supra* note 47, at 14, col. 1; Comment, *supra* note 46, at 563.

66. See Greene, *supra* note 47, at 14, col. 1; see also Comment, *supra* note 46, at 563. As the Swiss Federal Tribunal stated:

According to Section 21 of the Securities Exchange Act, the SEC has ample investigative powers, very similar to those of a normal police authority. If its investigations reveal some facts which may fall within the statutory provisions which punish the violation of stock trading rules, the SEC is also empowered to refer the matter to the Attorney-General who may in his discretion open a criminal investigation.

First Swiss Opinion, *supra* note 15, at 788.

67. See Mutual Assistance Treaty, *supra* note 20, at art. 4, para. 2(a) (referring to the Schedule of Offenses for which compulsory measures are available, in particular

These provisions, however, are only available if the SEC can persuade the Swiss government and banking authorities that at least one requirement of the Swiss penal law prohibits insider trading.⁶⁸

B. THE 1982 MEMORANDUM OF UNDERSTANDING BETWEEN THE UNITED STATES AND SWITZERLAND

The Memorandum of Understanding resolves any doubts concerning the Treaty's applicability to insider trading. It establishes mutual cooperation between the governments of the United States and Switzerland in pursuing violators of United States laws that prohibit insider trading.⁶⁹ This unprecedented agreement allows the SEC to obtain the identities of the Swiss bank customers whenever the SEC can prove it has a reasonable belief that inside trading has occurred through a Swiss bank.⁷⁰ The MOU, thereby, effectively ensures Swiss cooperation in SEC investigations despite the absence of specific criminal penalties for insider trading in Switzerland.⁷¹

Negotiations on the MOU began in March 1981 when representa-

item 19(a)). Item 19(a) states, in pertinent part: "[Fraud including:] obtaining . . . money or securities by false pretenses or by defrauding by means of deceit, falsehood, or any other fraudulent means." *Id.*

68. Jenckel & Rider, *supra* note 43, at 683-84, cols. 1-2 (suggesting that several articles of the Swiss Code of Obligations may be helpful in persuading the Swiss government and banking authorities that the Swiss Penal Law prohibits insider trading). For example, article 21 of the Code of Obligations may be applicable to insider trading in cases of blatant unfairness because it renders a transaction void when one party acquires an unfair advantage over another party through inequality or abuse of bargaining power. *Id.* at 683, col. 2. According to the Swiss Federal Tribunal, however, article 21 requires a very high standard of proof, making blatant unfairness by implication practically impossible to prove in most cases of insider trading. *Id.* at 683, col. 3. Article 41, which holds an individual liable for either negligently or intentionally encroaching on another's rights, also may apply in these situations. *Id.* Yet, article 41 would be applicable only when an insider's failure to disclose material nonpublic information that he had an obligation to disclose injures another. As Jenckel & Rider indicate, however, Swiss law does not require disclosure. *Id.* Thus, the authors suggest that the most beneficial regulation in Swiss law is article 754 of the Code of Obligations, which states: "All persons entrusted with the direction and management or control of the company's affairs are liable to the company, its shareholders and creditors for damage caused wilful or negligent failure to perform their duties." *Id.* at 683-34, col. 1 (providing the translation of the Swiss Code of Obligations-Schweizerisches Obligationenrecht [OR] art. 754).

Corporate inside information may be used only for corporate purposes because it is confidential. Thus, insiders who improperly reveal corporate inside information may breach their fiduciary duties to the corporation. Jenckel & Rider, *supra* note 43, at 684, col. 1. A shareholder, therefore, may be able to bring an action if insider trading activities directly damaged the corporation in question. *Id.*

69. SEC Release, *supra* note 18, at 5; Memorandum of Understanding, *supra* note 18; Greene, *supra* note 47, at 12, col. 1.

70. Memorandum of Understanding, *supra* note 18, at art. 3, para. 3.

71. *Id.* at art. 2.

tives of the United States and Swiss governments met in Berne, Switzerland to discuss the growing conflicts in securities law enforcement matters.⁷² During these discussions, the Swiss expressed concern about the SEC's use of rule 37 of the Federal Rules of Civil Procedure to compel discovery of customer identification in United States courts.⁷³ The Swiss delegation clearly expressed its position that the use of rule 37 motions by United States law enforcement agencies encroached upon Switzerland's sovereignty and that Swiss laws should be respected by the United States courts.⁷⁴ The Swiss delegation also informed the United States delegation of the intention of the Swiss government to outlaw insider trading, and proposed the provisional agreement for the interim.⁷⁵ While the Swiss preferred that the Mutual Assistance Treaty provide the primary remedy whenever possible, the Swiss recognized United States objections to existing ambiguities in the Treaty that, according to the United States delegation, undermined effective enforcement of the Treaty by the SEC and allowed inside traders to exploit United States markets to their advantage.⁷⁶

The United States and Swiss delegations acknowledged the undesirability of ongoing litigation to force Swiss banks to reveal customer records to the SEC.⁷⁷ Both delegations, therefore, assented to an agreement whereby the United States would discontinue rule 37 motions to obtain Swiss banking information. In return, the Swiss banking authorities, subject to subsequent approval by the Swiss government, prom-

72. Greene, *supra* note 47, at 15, col. 2.

73. *Id.* at 14-15. In order to compel discovery against a foreign or non-resident party, the opposing party must allege that the non-resident has sufficient contacts in the forum state to be subject to that state's jurisdiction; see *World-wide Volkswagen Corp. v. Woodson*, 444 U.S. 286 (1980). Thus, a federal court can order a nonresident party to allow discovery of the desired information under rule 37. FED. R. CIV. P. 37. Failure to comply with such a discovery order may result in severe sanctions imposed by the court, such as prohibiting the noncomplying party from participating in U.S. securities markets. *Id.*; see also *Securities and Exchange Comm. v. Banca Della Svizzera Italiana and Certain Unknown Purchasers of Call Options for the Common Stock of St. Joe Minerals Corp.*, 92 F.R.D. 111 (S.D.N.Y. 1981) (enforced a motion to compel discovery of the identity of a Swiss bank customer where the bank was subject to Swiss banking laws). Rule 37 therefore presents Swiss banks with a difficult choice: a Swiss bank can either follow with Swiss secrecy laws and be subject to U.S. penalties, or comply with the motion for discovery and violate the Swiss secrecy laws. Greene, *supra* note 47, at 14, cols. 3-4. Based on traditional principles of comity, the bank may assert that the SEC and the court must recognize the validity of Swiss bank secrecy laws, and thus, hopefully may avoid this dilemma. *Id.* See also *RESTATEMENT (SECOND) OF FOREIGN RELATIONS LAW* §§ 39(1), 40 (1965) (providing limitations on the exercise of enforcement jurisdiction).

74. Greene, *supra* note 47, at 15, col. 2.

75. *Id.*

76. *Id.*

77. *Id.*

ised to cooperate with the SEC by using informational procedures similar to those provided for in the Treaty.⁷⁸ Noting that this agreement was not binding on the Swiss Federal Tribunal,⁷⁹ the parties signed a memorandum of understanding on August 31, 1982, and thereby established formal guidelines for handling insider trading cases until the Swiss make insider trading a crime under Swiss law.⁸⁰

The MOU has resolved several problems with Swiss cooperation in insider trading investigations. First, the MOU states that "an investigation by the SEC should be considered an investigation for which assistance could be furnished (if the other requirements of the Treaty are met) as long as the investigation relates to conduct which might be dealt with by the criminal courts."⁸¹ Unlike the Mutual Assistance Treaty, therefore, Swiss assistance is available to the SEC under the MOU whether or not there is criminal prosecution by the Department of Justice.⁸²

Second, the MOU resolves the problem created by the Mutual Assistance Treaty wherein each nation is only obliged to render assistance when a particular offense "would be punishable under the law in the requested state if committed within its jurisdiction"⁸³

The parties agreed in Article II, paragraph (3)(b) of the MOU that insider trading may constitute fraud, unfaithful management, or disclosure of business secrets under certain circumstances.⁸⁴ In such instances, the transaction in question would be unlawful under the Swiss Penal Code,⁸⁵ rendering Swiss assistance compulsory under the Mutual

78. *Id.*

79. Béguin, *supra* note 16, at 10, 11.

80. Memorandum of Understanding, *supra* note 18; SEC Release, *supra* note 18.

81. Memorandum of Understanding, *supra* note 18, at art. 2, para. 3(a).

82. See *supra* note 65 and accompanying text (discussing problems with receiving Swiss cooperation under the Mutual Assistance Treaty, which only covers criminal matters, when the offense is insider trading, a civil matter).

83. Mutual Assistance Treaty, *supra* note 20, at art. 4, para. 2(a). The MOU states in paragraph 3(b) of Article II:

The 1977 Treaty requires that a particular offense be a crime under the laws of each nation in order for compulsory assistance to be required under the Treaty. The parties understand that transactions effected by persons in possession of material non-public information could be an offense under Articles 148 (fraud), 159 (unfaithful management), or 162 (violation of business secrets) of the Swiss Penal Code. As a result the parties will understand that it will often be possible for compulsory measures to be ordered under the Treaty in order to assist the SEC in obtaining information from the banks that executed the securities transactions in the United States that are the subject of the request for assistance.

Memorandum of Understanding, *supra* note 18, at art. 2, para. 3(b).

84. *Id.*

85. Attempts to enrich oneself by a false representation or denial of truth directed to another person, or through exploitation of another's mistaken beliefs are unlawful

Assistance Treaty.⁸⁶ The parties also agreed that the investigative mechanism of the Treaty should be used whenever feasible.⁸⁷

The United States and Swiss delegations further agreed that the MOU would not "modify or supercede any laws or regulations in force in the United States or Switzerland."⁸⁸ The accord, therefore, does not give Swiss bank customers the right to appeal in a United States court a Swiss bank's decision to disclose information pertaining to a customer's record or identity.⁸⁹

The second major aspect of the MOU describes understandings reached concerning a proposed private agreement (Swiss Bankers' Agreement) among members of the Swiss Bankers' Association (SBA).⁹⁰ The Swiss Bankers' Agreement establishes a procedure whereby the SEC may obtain information regarding insider trading effected through Swiss banks where compulsory assistance would not be available under the Mutual Assistance Treaty because the SEC could not demonstrate a violation of the Swiss Penal Code.⁹¹

Under the Swiss Bankers' Agreement, the SBA will appoint a Commission of Inquiry⁹² to assist the SEC in obtaining information when-

under Article 148(1) of the Swiss Penal Code. Schweizerisches Strafgesetzbuch [StGB] art. 148(1); Code pénal suisse [CP] art. 148(1); Codice penale svizzero [CP] art. 148(1). Article 159(1) prohibits anyone, who is legally or contractually obligated to protect the pecuniary interests of others, from impairing these interests. StGB art. 159(1); CP art. 159(1); Cp art. 159(1). Article 162 makes it unlawful for any person to reveal a manufacturing or commercial secret for personal profit when that person is legally or contractually bound to keep that secret. StGB art. 162; CP art. 162; Cp art. 162.

86. See *supra* notes 38-42 and accompanying text (detailing the conditions requiring compulsory assistance under the Mutual Assistance Treaty). Paragraph 3(b) of Article II of the MOU states that "it will often be possible for compulsory measures to be ordered under the Treaty in order to assist the SEC in obtaining information from the banks that executed the securities transactions in the United States . . ." Memorandum of Understanding, *supra* note 18, at art. 2, para. 3(b).

87. Memorandum of Understanding, *supra* note 18, at art. 2, para. 2.

88. *Id.* at art. 5, para. 1.

89. *Id.* at para. 2.

90. *Agreement XVI of the Swiss Bankers' Association with Regard to the Handling of Requests for Information from the Securities and Exchange Commission of the United States on the Subject of Misuse of Inside Information*, 14 SEC. REG. & L. REP. (BNA) No. 39, at 1740 (1982) [hereinafter cited as Swiss Bankers' Agreement]. The understandings of the United States and Switzerland with regard to the proposed Swiss Bankers' Agreement are contained in the Memorandum of Understanding, *supra* note 18, at art. 3. The Swiss Bankers' Agreement is binding only upon signatory banks. *Id.*

91. Memorandum of Understanding, *supra* note 18, at art. 3, para. 1.

92. Swiss Bankers' Agreement, *supra* note 90, at art. 2, para. 1. The SBA will appoint a Commission of Inquiry composed of three members and three deputies, none of whom may exercise an executive function in a company subject to the Federal Law on Banks and Savings Banks.

ever the SEC demonstrates "reasonable grounds"⁹³ for requesting assistance.⁹⁴ Yet, the failure of the SEC to meet the threshold criteria⁹⁵ will not necessarily result in a presumption that it does not have "reasonable grounds" to request assistance.⁹⁶ The SEC may submit other information⁹⁷ indicating that transactions in connection with an acquisition or business combination constitutes a violation of United States insider trading laws. The Commission of Inquiry then reviews the information submitted by the SEC to determine if "reasonable grounds" exist for requesting assistance.⁹⁸

If the Commission of Inquiry is satisfied that the SEC has "reasonable grounds" to seek an investigative report from a Swiss bank, it will require that the bank in question release the identity of the customers⁹⁹

93. *Id.* at art. 3, para. 1. The SEC may demonstrate reasonable grounds for requesting assistance when: (i) material price or volume movements have occurred with respect to trading in the securities during the twenty-five day period prior to the announcement or (ii) the SEC has other material indications that the transactions were made in violation of U.S. insider trading laws and (iii) the daily trading volume of the securities increased by fifty percent or more at any time during the twenty-five trading days before the announcement over the average trading volume during the period from the 90th day to the 30th day before the announcement or (iv) if the price of the securities varied at any time by more than fifty percent during the twenty five trading days before the announcement.

94. *Id.* at art. 3, para. 4. Under the terms of the Swiss Bankers' Agreement, the SEC does not request assistance directly from the Commission of Inquiry. Instead, the SEC requests that the United States Department of Justice address a written application for assistance to the Swiss Federal Office for Police Matters (FOPM). *Id.* at art. 1(a); *see also supra* note 46 and accompanying text. The FOPM then forwards the application for assistance and accompanying information to the Commission of Inquiry. Swiss Bankers' Agreement, *supra* note 90, at art. 3, para. 1.

95. Memorandum of Understanding, *supra* note 18, at art. 3, para. 3.

96. *Id.*

97. The SEC's application for assistance must be accompanied by: (1) specific identification of transactions involving a company's securities, or put or call options for a company's securities, made within twenty-five days prior to the announcement of the acquisition or business combination, Swiss Bankers' Agreement, *supra* note 90, at art. 3, para. 3; (2) confirmation from the SEC or the Department of Justice that it will give all evidence or appropriate summaries thereof in its possession and which it is free to reveal to the Commission of Inquiry when such evidence is materially relevant to the investigation, *Id.* at art. 3, para. 2; and (3) a pledge by the SEC not to reveal the information provided by the Commission of Inquiry except in connection with an SEC investigation or law enforcement action initiated by the SEC against alleged inside traders of a company's securities, or put or call options for a company's securities, in connection with the acquisition or business combination. *Id.* at art. 3, para. 5. The MOU also states that the information provided by the Commission of Inquiry may not be used as evidence in any other proceeding. Memorandum of Understanding, *supra* note 18, at art. 3, para. 3.

98. Memorandum of Understanding, *supra* note 18, at art. 3, para. 3; Swiss Bankers' Agreement, *supra* note 90, at art. 3, para. 4.

99. The bank notifies each customer, who has thirty days to supply the bank with information showing that he is not involved in any securities law violations. Swiss Bankers' Agreement, *supra* note 90, at art. 4, para. 2. This information, along with the

and the details of the transactions involved.¹⁰⁰ The Commission of Inquiry then supplies this information to the SEC through the Swiss Federal Office for Police Matters (FOPM), unless the bank's report establishes to the reasonable satisfaction of the Commission that the individual or individuals identified did not engage in insider trading or could not be involved in inside trading.¹⁰¹ If the accuracy of the report is in doubt, the SEC can ask the Swiss Federal Banking Commission to examine the report.¹⁰² If any material inaccuracy is found in an amended report, a report explaining the reasons for this determination must be sent to the SEC by the FOPM.¹⁰³

If the criteria of Article 1 and Article 3 of the Swiss Bankers' Agreement are met, the Commission of Inquiry then will order the bank to hold a sum equalling the profit allegedly made from insider trading in the customer's account, pending disposition of the inquiry by the SEC or the United States courts.¹⁰⁴ The Commission of Inquiry will release these funds if the SEC does not complete the inquisition properly, if the SEC consents to the release of the funds, or if proceedings in the United States result in a judgment in favor of the Swiss bank

name, address, and nationality of the customer, plus information concerning the transactions, is sent to the Commission of Inquiry within forty-five days of its request to the bank. *Id.* at art. 4, paras. 3, 4.

100. *Id.* at art. 4, paras. 1, 3. The bank is required to report such information: [i]f within twenty-five trading days prior to a public announcement ("Announcement") of (A) a proposed merger, consolidation, sale of substantially all of an issuer's assets or other similar business combination ("Business Combination") or (B) the proposed acquisition of at least 10% of the securities of an issuer by open market purchase, tender offer or otherwise ("Acquisition"), a customer gives to a bank an order to be executed in the United States securities markets for the purchase or sale of securities or put or call options for securities of any company that is a party to a Business Combination or the subject of an Acquisition ("Company"), the bank, upon an inquiry by the Federal Office for Police Matters, shall disclose to the appropriate authorities pursuant to this Agreement the information.

Id. at art. 1.

101. *Id.* at art. 5, para. 2. Swiss Bankers' Agreement, *supra* note 90, defines an insider as:

(a) a member of the board, an officer, an auditor, or a mandated person of the company [that is a party to a Business Combination or the subject of an Acquisition] or an assistant of any of them; or

(b) a member of a public authority or a public officer who in the execution of his public duty received information about an Acquisition or a Business Combination; or

(c) a person who on the basis of information about an Acquisition or a Business Combination received from a person described in (a) or (b) has been able to act for the latter or to benefit himself from inside information. *Id.*

102. *Id.* at art. 8.

103. *Id.*

104. *Id.* at art. 9, para. 1.

customer.¹⁰⁵

The MOU and the Swiss Bankers' Agreement, therefore, represent a significant step toward greater cooperation between the United States and Switzerland in investigating potential insider trading violations.¹⁰⁶ The MOU provides a mechanism through which information concerning insider trading previously protected by Swiss bank secrecy laws may be obtained by the SEC.¹⁰⁷ Most importantly, a showing of questionable price or volume fluctuations of a given security, as required by the Swiss Bankers' Agreement provides an easily demonstrable and objective precondition for Swiss assistance that alleviates the burden of establishing a violation of the Swiss Penal Code as required under the Mutual Assistance Treaty.¹⁰⁸

II. THE SANTA FE CASE

A. BACKGROUND OF THE CASE

On October 5, 1981, the Santa Fe International Corporation announced a \$2.5 billion merger agreement in which it would become a United States subsidiary of the state-owned Kuwait Petroleum Corporation (KPC).¹⁰⁹ The merger agreement included KPC's promised cash purchase of all of Santa Fe's outstanding stock for \$51 per share.¹¹⁰

105. *Id.* at art. 9, para. 3.

106. In the MOU, Switzerland agrees that inside trading impairs the integrity of United States capital markets and confers an unfair advantage upon persons who engage in such trading. Memorandum of Understanding, *supra* note 18, at art. 1, para. 2. Furthermore, the MOU states that insider trading is "considered dishonorable" in Switzerland. *Id.* At least one commentator, however, has found such attitudes to be only a recent development: "In Switzerland, for example, ten years ago profit from insider trading was not only considered to be quite all right, but it was sometimes openly justified as part of management remuneration . . . [r]ecently, however, in Zurich there have been efforts to outlaw insider trading by more than mere self-regulation." Hopt, *Insider Trading on the Continent*, 4 J. COMP. CORP. L. & SEC. REG. 379, 380 (1982).

107. Memorandum of Understanding, *supra* note 18. Banks will disclose information concerning customers' identities and transactions under certain circumstances covered by the MOU and the Swiss Bankers' Agreement. Swiss Bankers' Agreement, *supra* note 90, at art. 3.

108. 1969-70 *Hearings*, *supra* note 4, at 21 (statement of Robert N. Morgenthau, United States Attorney for the Southern District of New York). Morgenthau discusses the difficulty of making an "exceptionally strong showing" that conduct is unlawful under Swiss and U.S. law without access to bank records. In addition, the MOU avoids problems created by cantonal rules of civil procedure and replaces the requirement of a court order for bank disclosure with a system specifically designed for investigating insider trading. *Id.*

109. Wash. Post, Oct. 6, 1981, at 1, col. 3.

110. *Federal Response to OPEC's Country Investments in the United States (Part 2: Investment in Sensitive Sectors of the U.S. Economy; Kuwait Petroleum Corp. Takeover of Santa Fe International Corp.): Hearings Before a Subcomm. of the*

The day after the announcement of the merger, after forty-three minutes of trading on the New York Stock Exchange, the price of Santa Fe stock increased from \$24.75 per share to \$43.75 per share.¹¹¹ Due to an influx of orders that created an imbalance on the "buy side" of the market,¹¹² the company requested that trading in Santa Fe stock be halted on all stock exchanges on Friday, October 2, and on the day the merger was announced, Monday, October 5.¹¹³

While the \$19 per share price increase represented a 77% increase in the value of the stock, call option contracts¹¹⁴ increased at an even greater rate. Indeed, following the announcement of the merger agreement, the market for option contracts for Santa Fe stock rose 1,325%.¹¹⁵ Traders who sold options on or before October 1 without owning the underlying stock¹¹⁶ lost millions of dollars when they were forced to buy the Santa Fe stock at significantly higher prices for resale to the owners of the call option contracts.¹¹⁷

Immediately following the halt in trading, the New York Stock Exchange and the Pacific Stock Exchange began an investigation to determine which customers purchased call options and/or common stock preceding the announcement of the merger agreement on October 5. The investigation revealed considerable increases in trading volume in Santa Fe shares as well as "significant and unusual purchases of call options" which originated not only in the United States, but also from Swiss banks¹¹⁸ during the two-week period before trading in Santa Fe stock and options had halted.

*House Comm. on Gov't Operations, 97th Cong., 1st Sess. 47 (1981) [hereinafter cited as *Federal Response Hearings*].*

111. *Id.* at 65.

112. *Federal Response Hearings, supra* note 110, at 65. An imbalance on the buy side of the market means that the number of orders to buy stock in a company exceeds the number of orders to sell stock in that company so that there is an inability to trade the stock.

113. Reuters Ltd., Business News, Oct. 6, 1981 (available on NEXIS).

114. *Id.* A call option contract generally entitles the owner to buy one hundred shares of underlying common stock at a specified price at anytime during the life of the contract.

115. Fedders, *Policy Internationalized U.S. Capital Markets: Methods to Obtain Evidence Abroad*, 18 INT'L LAW. 89, 101 (1984). Before the announcement of the merger agreement, the options sold for \$1.00 per contract. When trading in Santa Fe stock resumed, these call option contracts were worth \$14.25 each. *Federal Response Hearings, supra* note 110, at 34.

116. *Federal Response Hearings, supra*, note 110, at 47-51 (discussing this practice, commonly known as writing "naked" options).

117. Wall St. J., Oct. 21, 1981, at 7, col. 1.

118. *Federal Response Hearings, supra* note 110, at 41. One Swiss banker entered orders to buy 2,000 option contracts representing 200,000 shares of common stock on the Pacific Stock Exchange. *Id.*

Under pressure from Congress,¹¹⁹ the SEC filed a complaint in the United States District Court for the Southern District of New York on October 26, 1981, against Certain Unknown Purchasers of the Common Stock of Santa Fe International Corporation.¹²⁰ The complaint alleged that between September 21 and October 1, 1981, the "unknown"¹²¹ defendant purchasers acquired 3,000 call option contracts, at a total cost of \$384,206 that could be exercised to purchase 300,000 shares of Santa Fe common stock.¹²² The SEC also alleged that the unknown purchasers bought 27,000 shares of Santa Fe securities at a cost of \$340,000.¹²³ Following the announcement of the merger agreement between Santa Fe and KPC on October 5, the value of the call option contracts increased by \$5,344,763 and the value of the securities increased to \$335,000.¹²⁴

On the same day the SEC filed the *Santa Fe* case, United States District Judge William C. Conner issued a temporary restraining order freezing \$5.2 million in profits that the SEC charged were made through illegal insider trading¹²⁵ and being held in the buyer's accounts in nine United States banks and brokerage houses.¹²⁶ The SEC charged that the unknown defendants directly or indirectly made their transaction through the nominal defendants which included Citibank, Morgan Guaranty Trust Company of New York, Drexel Burnham Lambert,

119. See *Federal Response Hearing*, *supra* note 110, at 67-71 (testimony by John R. Evans, Commissioner, Securities and Exchange Commission).

120. *SEC v. Certain Unknown Purchasers*, *supra* note 14.

121. The identity of one unknown purchaser, Faisal al Massoud al Fuhaid, a Kuwaiti businessman, was known at the time the SEC's suit was filed in October 1981. Wall St. J., July 23, 1984, at 27, col. 1.; Richard James French, et al. v. Faisal al Massoud al Fuhaid, et al., [1984 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 91, 551 (S.D.N.Y. June 25, 1984). In addition to the unknown purchasers, five Swiss banks, including Credit Suisse and Swiss Banking Corp., were named as nominal defendants. See generally Wall St. J. Oct. 27, 1981, at 2, col. 3; Wall St. J., Oct. 28, 1981, at 2, col. 3.

122. See *supra* note 114 and accompanying text (discussing call option contracts and their use in the *Santa Fe* case); see also *SEC v. Certain Unknown Purchasers*, *supra* note 14 (detailing the complaint filed by the SEC in the *Santa Fe* case).

123. *SEC v. Certain Unknown Purchasers*, *supra* note 14; Fedders, *supra* note 115, at 101.

124. Fedders, *supra* note 115, at 100-01.

125. *SEC v. Certain Unknown Purchasers*, *supra* note 14. The SEC's complaint alleged that the unknown purchasers violated the anti-fraud provisions of the Securities Exchange Act of 1934 "by effecting transactions in the common stock of, and options to purchase the common stock of Santa Fe while in possession of material non-public information relating to merger discussions, negotiations and proposals between Santa Fe and Kuwait Petroleum Corporation." *Id.*

126. *Id.* The freezing of profits related to suspect transactions in American banks has become the SEC's primary weapon against insider trading.

Inc., Chase Manhattan Bank, and Credit Suisse.¹²⁷ Furthermore, the SEC argued for a temporary restraining order to prevent any assets derived from insider trading from leaving the United States,¹²⁸ while seeking a permanent injunction against the antifraud violations which would freeze the profits earned from these transactions.

B. THE SEC'S REQUEST FOR SWISS ASSISTANCE

With the funds safely frozen in New York, the SEC attempted to determine the identities of the unknown persons who traded the Santa Fe stock and options on the basis of inside information.¹²⁹ In March 1982, after lengthy discussions with the defendants' counsel and the government of Switzerland,¹³⁰ the United States Department of Justice, acting on behalf of the SEC, issued a formal request to the Swiss Federal Office for Police Matters for judicial assistance in identifying the unknown purchasers.¹³¹ According to the SEC request, the unknown defendants violated section 10(b) and rule 10b-5 of the Security Exchange Act of 1934¹³² while privy to material nonpublic information concerning the merger negotiations between Santa Fe and KPC.¹³³ The SEC argued that these offenses violated articles 148, 159, and 162 of the Swiss Penal Code.¹³⁴ Relying on these provisions, the SEC requested that certain witnesses be required to testify and that the Swiss banks in question release the requested information relating to insider trading in the *Santa Fe* case.¹³⁵

On April 2, 1982, the FOPM relayed the SEC's request for assistance to the senior member of the investigating magistrate of the Canton of Geneva and to the Office of the Public Prosecutor of the Canton of Zurich pursuant to article 10 of the Mutual Assistance Treaty.¹³⁶

127. *SEC Charges Santa Fe Int'l Stock, Option Buyers Used Nonpublic Information to Reap Illegal Profits*, [July-Dec.] SEC. REG. & L. REP. (BNA) No. 626, at A-1 (Oct. 28, 1981).

128. *Id.*

129. Nat'l L.J., Nov. 30, 1981, at 26, col. 1.

130. Fedders, *supra* note 115, at 101.

131. *First Swiss Opinion*, *supra* note 15, at 785-86.

132. Securities Exchange Act of 1934, *supra* note 1.

133. *First Swiss Opinion*, *supra* note 15, at 786. The request also stated that the alleged offenses may have included mail fraud. *Id.* The United States apparently was unable to substantiate this claim, which was not addressed by the Swiss Federal Tribunal. *Id.*

134. *Id.*; see also *supra* note 85 and accompanying text (discussing offenses that are unlawful under the Swiss Penal Code).

135. *First Swiss Opinion*, *supra* note 15, at 786.

136. *Id.* at 787. Article 10 of the Mutual Assistance Treaty states in part:

1. A person whose testimony or statement is requested under this Treaty shall be compelled to appear, testify and produce documents, records and articles of evi-

The FOPM rejected the notion that the administrative or civil aspects of the SEC's suit prevented consideration of the request for assistance and issued a decision concluding that the request met the requirements of the Mutual Assistance Treaty.¹³⁷ A bank customer subsequently appealed the FOPM's order under article 16 of the Treaty.¹³⁸ On June 30, 1982, the FOPM denied this initial appeal of its decision.¹³⁹ Following the FOPM's denial, the bank customer appealed to the Swiss Federal Tribunal.¹⁴⁰

C. THE FIRST OPINION OF THE SWISS FEDERAL TRIBUNAL

On January 26, 1983, after the signing of the MOU between the United States and Switzerland,¹⁴¹ the Swiss Federal Tribunal upheld the claim of the petitioner (the unidentified appellant bank customer) who previously had appealed the decision of the FOPM granting the SEC's request for Swiss assistance under the Mutual Assistance Treaty.¹⁴² The decision of the Swiss Federal Tribunal reversed the findings of the FOPM and denied the SEC's formal request for assistance under the treaty which, in turn, forced the SEC to explore alternative strategies for obtaining Swiss banking information in the *Santa Fe*

dence in the same manner and to the same extent as in criminal investigations or proceedings in the requested State. Such person may not be so compelled if under the law in either State he has a right to refuse. If any person claims that such a right is applicable in the requesting State, the requested State shall, with respect thereto, rely on a certificate of the Central Authority of the requesting State.

Mutual Assistance Treaty, *supra* note 20, at art. 10, para. 1. Requests for assistance are handled by a Central Authority in each country. For the United States, the Central Authority is the Attorney General or his appointee. For Switzerland, the Central Authority is the Division of Police of the Federal Department of Justice and Police in Berne. *Id.* at art. 28.

137. *First Swiss Opinion*, *supra* note 15, at 787.

138. *Id.* Article 16 of the Mutual Assistance Treaty states:

1. Upon request, the requested State shall make available to the requesting State on the same conditions and to the same extent as they would be available to authorities performing comparable functions in the requested State the following documents and article:

(a) judgments and decisions of courts; and (b) documents, records, and articles of evidence, including transcripts and official summaries of testimony, contained in the files of a court or an investigative authority, whether or not obtained by grand juries.

Mutual Assistance Treaty, *supra* note 20, at art. 16, para. 1.

139. *First Swiss Opinion*, *supra* note 15, at 787.

140. *Id.*

141. *See supra* notes 69-108 and accompanying text (discussing 1982 MOU between the United States and Switzerland).

142. *See supra* notes 136-40 and accompanying text (discussing the appeal of the FOPM decision).

case.¹⁴³

The Swiss Federal Tribunal began its opinion by stating that the SEC, through the United States Department of Justice, has "ample investigative powers"¹⁴⁴ to request judicial assistance under the treaty.¹⁴⁵ Based on section 10(b) and rule 10b-5,¹⁴⁶ the court then rejected petitioner's argument that insider trading "cannot constitute a criminal offense and be prosecuted in the United States."¹⁴⁷

Although insider trading is "generally reprobated and considered as morally offensive,"¹⁴⁸ the Swiss Federal Tribunal noted that it is not considered a criminal offense under the Swiss Penal Code.¹⁴⁹ The court then examined whether the criminal offenses of unfaithful management, fraud, or violation of business secrets were committed by the insider trading that took place in the *Santa Fe* case. After considering each offense, the court found insufficient evidence to prove that crimes had been committed under the Swiss Penal Code.

First, the Swiss Federal Tribunal considered whether the crime of unfaithful management had been committed under article 159 of the Swiss Penal Code. The court held that in this case the unknown purchasers of stocks and options owed no legal or contractual duty to the sellers, with whom no prior relationship existed.¹⁵⁰ While an insider may owe a duty to the company for which he has inside information, no offense is committed under article 159 when no harm is done to the financial interests of the company itself.¹⁵¹ In this case, the court found that neither Santa Fe nor KPC sustained any damage as a result of the transaction in question.¹⁵²

The court then examined the question of fraud. Article 148 of the Swiss Penal Code defines fraud as the abuse of another by false state-

143. *First Swiss Opinion, supra* note 15, at 787.

144. *Id.* at 788. The SEC derives its investigatory authority from § 21 of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78u(a), 78hh (1982).

145. *First Swiss Opinion, supra*, note 15, at 787-88. The Swiss Federal Tribunal stated that "[a]ccording to Section 1(1)(a) of the [Mutual Assistance] Treaty, Switzerland must grant the requests for judicial assistance made during investigations or judicial proceedings related to offenses, the prosecution of which falls within the jurisdiction of the requiring State or one of its member States." *Id.* at 787; *see also* Mutual Assistance Treaty, *supra* note 20, at art. 1, para. 1(a).

146. *In re Cady, Roberts & Co., supra* note 2, at 907, 912.

147. *First Swiss Opinion, supra* note 15, at 789.

148. *Id.* at 792; *see also supra* note 106 (quoting similar language in MOU).

149. *First Swiss Opinion, supra* note 15, at 792; *see also* note 85 and accompanying text (quoting Article 148(1) of Swiss Penal Code).

150. *First Swiss Opinion, supra* note 15, at 792.

151. *Id.*

152. *Id.*

ments or by hiding facts in order to enrich oneself or a third party.¹⁵³ Exploitation of another's mistaken beliefs by inducing a person to act contrary to his or her own financial interests or to those of a third party also is considered fraud for purposes of article 148.¹⁵⁴ The Swiss Federal Tribunal rejected the applicability of article 148 to insider trading for several reasons. First, the court held that "only the exploitation of a pre-existing error in an insider transaction may meet the requirements of article 148."¹⁵⁵ Article 148, therefore, is violated only when a person uses another's "error" or "mistake of fact" to cause "the deceived person to act detrimentally against his own or another's property."¹⁵⁶ In the *Santa Fe* case, the SEC argued that the general lack of knowledge among stock and option traders of the impending merger between Santa Fe and KPC constituted such error or mistake of fact.¹⁵⁷

The Swiss Federal Tribunal determined that because an insider has no personal contact of relationship with his "victim" on a stock exchange, there is no duty to disclose prior to trading.¹⁵⁸ In fact, the court reasoned that had the insider not acted, the victim still would have concluded the transaction in question with a third party, and therefore, would have ended up in the same financial condition.¹⁵⁹ Thus, the Swiss Federal Tribunal concluded that an insider who trades with privileged information is not responsible for the other's losses be-

153. *Id.* at 792-93; see also *supra* note 85 and accompanying text (discussing violations under article 148(1) of the Swiss Penal Code).

154. *Id.*

155. *Id.*

156. Schweizerisches Strafgesetzbuch [StGB] art. 148. Article 148 of the Swiss Criminal Code states:

Any person who, with intent to make an unlawful profit for himself or another, shall fraudulently mislead another person by falsely representing or concealing facts or shall fraudulently use the error of another and thus cause the deceived person to act detrimentally against his own or another's property, shall be confined in the penitentiary for not more than five years or in the prison. The offender shall be punishable with a penitentiary term of not over ten years and fined if he makes a business of committing frauds. Defrauding a relative or a member of (one's) own family shall be prosecuted on petition only.

Id.; see also Friedlander & Goldbert, *The Swiss Federal Criminal Code*, 30 J. CRIM. L. & CRIMINOLOGY 1 (1939-40) (Supp.) (translating the Swiss Federal Criminal Code into English); *supra* note 85 and accompanying text (discussing a similar provision in the Swiss Penal Code).

157. *First Swiss Opinion*, *supra* note 15, at 793-94.

158. *Id.*; see also *supra* notes 85 and 156 and accompanying text (discussing Article 148 of Swiss Criminal Code).

159. *First Swiss Opinion*, *supra* note 15 at 795. This reasoning ignores the accepted finding that insider trading activity can cause a substantial rise in the volume of trading. See Memorandum of Understanding, *supra* note 18; Swiss Bankers' Agreement, *supra* note 90.

cause insider trading itself causes no injury.¹⁶⁰ Accordingly, the court found that insider trading in the instant action did not constitute fraud as defined in article 148.

Finally, the court considered whether article 162 of the Swiss Penal Code, which makes the disclosure of business secrets a crime, applied to this case.¹⁶¹ While noting that the "preparation of a merger" is considered a business secret, the Swiss Federal Tribunal found that article 162 is not violated when a person makes use of privileged information for his own profit without disclosing the information to a third party.¹⁶² The stock transactions involved in the *Santa Fe* case would, therefore, fall within the meaning of article 162 only if carried out on the basis of a disclosure of the merger plan.¹⁶³ Since the request for judicial assistance did not indicate whether those suspected of insider trading acted alone or disclosed their inside information to third parties, the SEC failed to establish a factual basis for a possible violation of article 162.¹⁶⁴

The Swiss Federal Tribunal, therefore, held that the alleged insider trading in the *Santa Fe* case did not include elements of unfaithful management or fraud under the Swiss Penal Code. Furthermore, the United States request for judicial assistance did not provide sufficient evidence to demonstrate a possible disclosure of business secrets in violation of Swiss law. Based on these findings, the court ordered the FOPM to deny the SEC's request for assistance.¹⁶⁵

The decision of the Swiss Federal Tribunal is instructive insofar as it resolves the issue of whether the SEC can use the Mutual Assistance Treaty to combat illegal insider trading in the United States.¹⁶⁶ The Treaty states that the United States Department of Justice must file all requests for assistance with the FOPM whether the offense under investigation is civil or criminal.¹⁶⁷ According to this decision, the SEC

160. *First Swiss Opinion, supra* note 15, at 795. The Swiss Federal Tribunal also stated that because the insider:

sells or purchases said stocks or options at the price as quoted by the stock exchange and the insider's behavior, i.e., his deriving a profit from privileged information, in no way constitutes the primary and direct cause of any subsequent fluctuations of the prices as quoted at the stock exchange.

Id.

161. *Id.* at 796.

162. *Id.*

163. *Id.* at 797.

164. *Id.* at 796-98.

165. *Id.* at 797-98.

166. *Id.* at 789.

167. *See Greene, supra* note 47, at 14, col. 1; *see also supra* notes 65 and 94 and accompanying text.

may obtain investigative assistance under the Treaty for civil prosecutions even though the Department of Justice might not prosecute the offense criminally.¹⁶⁸

The difficulties that the SEC experienced in attempting to implement the Mutual Assistance Treaty to obtain judicial assistance in investigating insider trading in the *Santa Fe* case demonstrated the need for a more accurate delineation of the SEC's right to pursue inside traders. In the meantime, however, the SEC had to find alternative methods of obtaining Swiss banking information.

D. THE SEC'S SECOND REQUEST FOR SWISS ASSISTANCE

On June 20, 1983, John Fedders, the SEC Director of Enforcement, announced in an interview that "in the past couple of weeks . . . [the SEC] had some remarkable breaks" in investigating the *Santa Fe* case, which by that time had become one of the largest insider trading probe in the SEC's history.¹⁶⁹ Specifically, SEC investigators believed that they discovered the names of seven to eight inside traders who bought stock in Santa Fe through Swiss banks before the public announcement of the merger agreement with KPC in 1981.¹⁷⁰ Armed with this new information,¹⁷¹ SEC officials stated that they planned to renew the SEC's request for Swiss assistance.¹⁷²

On August 16, 1983, an official in the Swiss Justice Ministry confirmed that the United States Department of Justice had again sought Swiss assistance in the *Santa Fe* case.¹⁷³ On November 29, 1983, the Swiss Federal Tribunal declined to rule, as the banks involved in the *Santa Fe* case had requested, that the Swiss authority was not empowered to represent the United States in its efforts to obtain information regarding suspected Swiss bank accounts of inside trade.¹⁷⁴ According to a Swiss embassy official in Washington, D.C., the Swiss Federal Tri-

168. *First Swiss Opinion*, *supra* note 15, at 788-89.

169. Wall St. J., June 10, 1983, at 12, col. 2; *see also supra* note 32 and accompanying text. The largest insider trading case filed by the SEC was the Levine case. N.Y. Times, May 15, 1986, at 27, col. 3; *see supra* note 19 and *infra* note 199 (providing the background of the Levine case).

170. Wall St. J., June 10, 1983, at 12, col. 2.

171. *Id.* Fedders declined to say how the SEC discovered its new information, or to say anything about the bank clients, aside from the fact that they numbered seven or eight. *Id.*

172. *Id.*

173. Reuters Ltd., Business News, Aug. 16, 1983 (available on NEXIS).

174. *Banks' Request in Santa Fe Case Rejected by Swiss Court*, 15 SEC. REG. & L. REP. (BNA) No. 48, at 2239 (Dec. 9, 1983). The banks involved were Credit Suisse, Lombard, Odier & Cie of Geneva, Swiss Bank Corp., and the Swiss branches of the Chase Manhattan Bank and Citibank. *Id.*

bunal's one page opinion discussed a procedural issue raised by the banks which argued that the United States request for assistance amounted to a "revision" of the prior United States request that the court had previously rejected.¹⁷⁵

The second United States request expressly sought information regarding tipping activity.¹⁷⁶ "Tipping" occurs when one person discloses non-public information regarding an impending transaction (in this case, the merger between KPC and Santa Fe) to another person.¹⁷⁷ Tipping violates article 162 of the Swiss Penal Code which prohibits the disclosure of business secrets.¹⁷⁸ The United States, therefore, needed to supply enough evidence to the Swiss government to prove that third parties had received inside knowledge in violation of article 162.¹⁷⁹

E. THE SECOND OPINION OF THE SWISS FEDERAL TRIBUNAL

On May 16, 1984, the Swiss Federal Tribunal ordered five Swiss banks to divulge the identities of the previously unknown inside traders.¹⁸⁰ The ruling marked the first time the Swiss ever provided such assistance to SEC investigators.¹⁸¹ Lawrence Chamblee, an attorney for the Department of Justice Office of International Affairs, said that the decision would "signal to those who would trade on the basis of inside information that Swiss bank secrecy is no longer available as a shield from SEC investigations."¹⁸²

The Swiss Federal Tribunal began its decision by acknowledging the necessity of reviewing the SEC's second request. According to the court, the United States now sought to demonstrate that the unknown purchasers of shares or options of Santa Fe did not obtain inside information through their employment or affiliation with Santa Fe, but rather, through third parties who knew of the pending merger announcement.¹⁸³ The court stated that the SEC probably obtained the new facts either through the ordinary investigative proceedings, or

175. *Id.*

176. *Id.*

177. *Id.*

178. *See supra* notes 161-64 and accompanying text (discussing article 162 of Swiss Penal Code).

179. Reuters Ltd., Business News, Aug. 16, 1983 (available on NEXIS); *see Second Swiss Opinion, supra* note 15, at 748 (discussing the information provided to the Swiss government).

180. Wall St. J., May 17, 1984, at 3, col. 1.

181. *Id.*

182. *Id.*

183. *Second Swiss Opinion, supra* note 15, at 754.

through confidential proceedings, some of which may have involved inside traders who collaborated closely with United States authorities.¹⁸⁴ Because the SEC's second request concerned disclosure of business secrets, a violation of article 162 of the Swiss Penal Code,¹⁸⁵ the requirements of paragraph 2(a) of article 4 of the Mutual Assistance Treaty¹⁸⁶ were satisfied, and thus, the Swiss could begin to assist in the *Santa Fe* investigation.¹⁸⁷

As a result of the ruling of the Swiss Federal Tribunal, the five Swiss banks¹⁸⁸ involved in the *Santa Fe* investigation turned over the suspected inside traders' bank account records, order tickets, and other documents.¹⁸⁹ Although the decision forced the release of the names of five suspected inside traders,¹⁹⁰ the defendants appealed the decision to several Swiss political bodies with jurisdiction over the matter.¹⁹¹ During this time, the SEC could not obtain further documentary evidence with respect to the unknown purchasers.¹⁹²

F. FINAL RESOLUTION OF THE SANTA FE CASE

On February 20, 1985, the Swiss Federal Council¹⁹³ rejected an appeal by unidentified customers of Swiss banks who attempted to block the release of key bank documents to the SEC pursuant to the May 1984 decision of the Swiss Federal Tribunal.¹⁹⁴ In its ruling, the Swiss Federal Council stated that release of the requested information would not be detrimental to the national interest.¹⁹⁵ While the Swiss Federal Council was the last body with jurisdiction to hear this case,¹⁹⁶ the de-

184. *Id.*; see *supra* note 170-71 and accompanying text (discussing the discovery of names of inside traders by the SEC).

185. See *supra* notes 161-64, 177 and accompanying text (discussing violations under article 162 of the Swiss Penal Code).

186. See *supra* notes 38-42 and accompanying text (discussing the requirements of the Mutual Assistance Treaty).

187. *Second Swiss Opinion*, *supra* note 15, at 753-55.

188. See *supra* note 174 (listing the five Swiss banks).

189. Wall St. J., May 17, 1984, at 3, col. 2.

190. *Swiss Government Agrees to Give SEC Key Data in Santa Fe Insider Probe*, 17 SEC. REG. & L. REP. (BNA) No. 8, at 327 (Feb. 22, 1985).

191. *SEC v. Certain Unknown Purchasers*, FED. SEC. L. REP. (CCH) ¶ 91, 951 (S.D.N.Y. Feb. 20, 1985).

192. *Id.*

193. *Second Swiss Opinion*, *supra* note 15, at 747 n.8. The Swiss Federal Council is the executive branch of the Swiss Government. It consists of seven members elected by the Swiss Parliament. *Id.*

194. *SEC v. Certain Unknown Purchasers*, FED. SEC. L. REP. (CCH) ¶ 91, 951 (S.D.N.Y. Feb. 20, 1985).

195. *Swiss Government Agrees to Give SEC Key Data in Santa Fe Insider Probe*, 17 SEC. REG. & L. REP. (BNA) No. 8, at 327 (Feb. 22, 1985).

196. *SEC v. Certain Unknown Purchasers*, FED. SEC. L. REP. (CCH) ¶ 91, 951

cision, announced in Berne and confirmed by the SEC, went officially unreported.¹⁹⁷ Armed with new information concerning the unknown purchasers, the SEC began piecing together the inside trading activities involving Santa Fe securities that occurred prior to the public announcement of the merger agreement between Santa Fe and KPC in 1981.

Ultimately, on February 26, 1986, United States District Judge William C. Conner approved final settlement in the *Santa Fe* case.¹⁹⁸ In one of the SEC's largest settlements ever, eight foreign investors accused of insider trading in Santa Fe securities agreed to turn over \$7.8 million in profits to a special claims fund to reimburse investors who lost money in Santa Fe trading in 1981.¹⁹⁹

It is interesting to note that the Swiss Federal Tribunal concluded in its January 1983 opinion that there were no "victims" in the *Santa Fe* case because the "victimized" traders still would have concluded the transactions in question with third parties even if the insiders had not acted.²⁰⁰ While there is some merit to this argument, the United States Congress declared insider trading illegal in part "to protect honest enterprise, seeking capital by honest presentation, against the competition afforded by dishonest securities offered to the public through crooked promotion."²⁰¹ The SEC, therefore, believes that the return of the money lost by honest investors in the *Santa Fe* case will deter future

(S.D.N.Y. Feb. 20, 1985).

197. Letter to the author from Carmen M. Sommer, associate attorney with the law firm of Froriep, Renggli & Partner, in Zurich, Switzerland (Sept. 17, 1985).

198. See Wall St. J., Feb. 27, 1986, at 3, col. 2; N.Y. Times, Feb. 27, 1986, at 33, col. 1 (discussing the settlement of the *Santa Fe* case).

199. Wall St. J., Feb. 27, 1986, at 3, col. 2. The SEC stated that the \$7.8 million settlement was the largest sum it had ever forced individuals in an insider trading case to repay. N.Y. Times, Feb. 27, 1986, at 33, col. 1.

In the *Levine* case, which was even larger than the *Santa Fe* case, the SEC required that inside trader Levine return \$10.6 million in profits and pay additional imposed penalties on the illegal profits. See *supra* note 19 (providing the background of the *Levine* case); see also Gilpin, *\$5 Million Bail Set on S.E.C. Charges*, N.Y. Times, May 14, 1986, at 30, col. 5 (discussing the high bail set for Levine corresponding to his high level of profit). Several million dollars of this settlement are likely to be used to cover back taxes assessed when Levine was purchasing on inside information. N.Y. Times, June 6, 1986, at 1, col. 1. Money will also be used to repay investors who sold stocks Levine was purchasing on inside information. The SEC hopes that the deprivation of all monetary gain, in addition to penalties, will deter the increasing number of inside traders. *Id.*

200. *First Swiss Opinion, supra* note 15, at 795; see also *supra* notes 158-60 and accompanying text (discussing Swiss interpretation of insider trading laws).

201. *United States v. Naftalin*, 441 U.S. 768, 775-76 (1979) (quoting S. Rep. No. 47, 73d Cong., 1st Sess. 1 (1933)); see also *supra* note 7 and accompanying text (discussing legislative intent regarding the adoption of the Securities Exchange Act of 1934).

investors from engaging in illegal insider trading activities, and thus, will advance further Congress' goals embodied in the Securities Exchange Act.

According to the SEC, the eight foreign investors²⁰² learned of KPC's impending takeover of Santa Fe in 1981 from Costandi Nasser, a Lebanese businessman.²⁰³ Nasser used several Swiss bank accounts in his own name and in the name of the Rachanal Foundation, a concern under his control, to buy Santa Fe options.²⁰⁴ Nasser, who allegedly made \$3.5 million on the transactions, in turn, learned of the merger through a business associate, Darius Keaton, who was then a director of Santa Fe.²⁰⁵ Keaton, who bought 10,000 shares of stock through a Swiss bank account he kept under the name of Nadir Katir Mabrouk, settled the civil charges against him in September 1982.²⁰⁶ While Keaton neither admitted nor denied committing securities law violations, he was required to give up more than \$300,000 in profits and enjoined from any fraud violations in the future as part of his settlement with the SEC.²⁰⁷

Six of the eight foreign investors accused of insider trading by the SEC, without admitting or denying the charges, consented to the injunction signed by Judge Conner enjoining them from committing fraud violations in the future.²⁰⁸ Sheikh Khalid bin Hamad al Thani, interior minister of Qatar, and A.R. Mannai, owner of a Qatar trading company, did not consent to the injunction but agreed to give up trading profits of \$375,333 and \$563,815 respectively.²⁰⁹

CONCLUSION

The final and successful resolution of the *Santa Fe* case represents a major breakthrough in the enforcement of United States securities laws by the SEC. Prior to the Mutual Assistance Treaty, the MOU, and the

202. The eight investors involved were: Costandi Nasser, a Lebanese businessman; Faisal al Massoud al Fuhaid, a Kuwaiti businessman; Luay Tewfik al Swaidi, an Iraqi living in London; Hildebrand R. H. McCulloch, a former employee of a Santa Fe subsidiary living in London; Sonawel Anstalt; the Rachanal Foundation of Liechtenstein; Sheik Khalid bin Hamad al Thani, the Interior Minister of Qatar; and A. R. Mannai, owner of a Qatar trading company. N.Y. Times, Feb 27, 1986, at 40, col. 1.

203. Wall St. J., Feb. 27, 1986, at 3, col. 2.

204. *Id.*

205. *Id.*

206. *Id.*; see also *supra* note 17 and accompanying text (discussing the settlement of cases with the SEC).

207. See Wall St. J., Sept. 30, 1982, at 8, col. 3; Wall St. J., Feb. 27, 1986, at 3, col. 2 (discussing Keaton's settlement with the SEC).

208. Wall St. J., Feb. 27, 1986, at 3, col. 2.

209. *Id.*

two decisions of the Swiss Federal Tribunal in the *Santa Fe* litigation, Switzerland's traditional, and seemingly impenetrable, veil of bank secrecy afforded a means by which to trade options and securities based on inside information without fear of detection. Yet, the final resolution of the civil litigation in the *Santa Fe* case shows that the Mutual Assistance Treaty and the MOU are effective instruments for uncovering evidence of alleged insider trading that otherwise would remain concealed under Switzerland's strict bank secrecy laws. As Gary Lynch, SEC Director of Enforcement, stated, "[The *Santa Fe*] case demonstrates [the SEC's] commitment to go anywhere to get the facts necessary to prosecute securities law violators."²¹⁰

According to the SEC, the final settlement of the *Santa Fe* case sets a precedent for international cooperation in future cases of this kind.²¹¹ Michael Mann, chief of the SEC's Office of International Legal Assistance, claimed such efforts to combat insider trading would become increasingly important to the SEC because of the growing internationalization of the securities market.²¹² Mann said that two areas of great abuse of inside information occurred in the use of stock options and international networks.²¹³ Thus, the resolution of the *Santa Fe* litigation, according to Mann, helped reduce access to some of these international loopholes.²¹⁴

Indeed, the successful completion of the *Santa Fe* case represents an important precedent for cooperation in law enforcement between the United States and Switzerland. Given the increasing importance of international markets, therefore, such cooperation has become necessary in order to eradicate the presence of inside traders in United States securities markets.

210. *Id.*

211. N.Y. Times, Feb. 27, 1986, at 40, col. 2.

212. *Id.*

213. *Id.*

214. *Id.*