

## **The Good and the Bad of Insider Trading**

Anyone who has seen the movie "Wall Street" has no doubt heard the term "insider trading." Additionally, with many well known people, such as Martha Stewart back in 2004, getting caught up in this sometimes illegal act, insider trading is a term that is not uncommon among investors. However, what is uncommon is the belief that all insider trading is always illegal. But, as I used to tell my clients when I was a stock broker, as with many other things in life, insider trading has its good and its bad.

### **The Good**

There are many times that an insider, such as an officer of a company, may buy or sell shares and have it be perfectly legal. In order to do so, the insider must not be trading on information that is non-public and they must also file special forms with the Securities and Exchange Commission (SEC). Most of the time when insiders are selling it is on a scheduled plan and many times the same holds true for buying as well.

### **The Bad**

Insider trading that is done using information that is not public knowledge is illegal insider trading. Typically an insider is an officer of a company, but an insider can also be someone who has the same inside information as a company insider would have. For example, if the CEO of XYZ Corp sells a large block of his personal shares because he knows that a bad financial report is due to come out in a couple of days, then they are guilty of insider trading. But what if that CEO happened to mention the upcoming bad report to his college buddy and that friend decides to sell his shares of XYZ Corp ahead of time? Because the college buddy possessed information that was privy only to those inside the company and that information was not yet public knowledge, he too would be guilty of insider trading.

### **Why Insiders Can't Use Non-Public Information**

Insiders who use non-public information in order to get a leg up on a stock trade are said to be in breach of their fiduciary responsibilities. In other words, they have a great secret and they are not allowed to use that secret to profit; that would be like cheating. This would certainly not be in the best interest of the company's stockholders, who are supposed to be number one on a company officer's agenda, and so the practice is heavily regulated to keep a lid on the illegal side of insider trading.