EXAMINING STOCK TRADING REFORMS FOR CONGRESS

HEARING

BEFORE THE

COMMITTEE ON HOUSE ADMINISTRATION
HOUSE OF REPRESENTATIVES

ONE HUNDRED SEVENTEENTH CONGRESS

SECOND SESSION

APRIL 7, 2022

Printed for the use of the Committee on House Administration

Available on the Internet:
http://www.govinfo.gov/committee/house-administration

EXAMINING STOCK TRADING REFORMS FOR CONGRESS

EXAMINING STOCK TRADING REFORMS FOR CONGRESS

HEARING

BEFORE THE

COMMITTEE ON HOUSE ADMINISTRATION
HOUSE OF REPRESENTATIVES

ONE HUNDRED SEVENTEENTH CONGRESS

SECOND SESSION

APRIL 7, 2022

Printed for the use of the Committee on House Administration

Available on the Internet:
http://www.govinfo.gov/committee/house-administration

U.S. GOVERNMENT PUBLISHING OFFICE

47–699 WASHINGTON : 2022

CONTENTS

April 7, 2022

EXAMINING STOCK TRADING REFORMS FOR CONGRESS

THURSDAY, APRIL 7, 2022

HOUSE OF REPRESENTATIVES,
COMMITTEE ON HOUSE ADMINISTRATION,
Washington, DC.

The Committee met, pursuant to other business, at 9:09 a.m., in Room 1310, Longworth House Office Building, Hon. Zoe Lofgren [Chairperson of the Committee] presiding.

Present: Representatives Lofgren, Butterfield, Aguilar, Scanlon, Davis, Loudermilk, and Steil.

Staff Present: Jamie Fleet, Democratic Staff Director; Khalil Abboud, Deputy Democratic Staff Director; Caleb Hays, Minority General Counsel and Deputy Staff Director; Dan Taylor, Senior Counsel; Kulani Jalata, Elections Counsel; Sean Jones, Professional Staff Member; Andrew Garcia, Staff Assistant; Tim Monahan, Minority Staff Director; Elliot Smith, Minority Professional Staff Member; Kyle Parker, Chief of Staff for Representative Butterfield; and Elizabeth Arevalo, Legislative Director for Representative Leger Fernandez.

OPENING STATEMENT OF HON. ZOE LOFGREN, CHAIRPERSON

The CHAIRPERSON. The Committee on House Administration will come to order. I want to say good morning to everyone.

As we begin, I want to note, we are holding this hearing in person but also in compliance with the regulations for Remote Committee Proceedings pursuant to House Resolution 8. Members and witnesses were provided an opportunity to participate remotely if necessary. None of the witnesses are doing so for this proceeding. And, of course, we have the Members who are here at the dais personally. I am very pleased to see everyone here. I note that we are holding this hearing in compliance with the most recent guidance issued by the Office of the Attending Physician.

At this time, I ask unanimous consent the chair be authorized to declare a recess of the Committee at any point and that all Members have five legislative days in which to revise and extend their remarks and have any written statements be made part of the record.

And, hearing no objections, that is so ordered.

The CHAIRPERSON. For all of us who are fortunate enough to work in public service, a guiding principle should be that a public office is a public trust. Without the public's trust and confidence, government loses its legitimacy.

That principle was of paramount importance to the Founders. As "The Federalist Papers" put it, "The aim of every political constitution is, or ought to be, first to obtain for rulers men who possess—I would add women as well—most wisdom to discern, and most virtue to pursue, the common good of the society; and in the next place, to take the most effectual precautions for keeping them virtuous whilst they continue to hold their public trust."

Since the founding, this has remained a vital underpinning of our democracy and informed periodic reforms to address shortcomings in standards of conduct for public officials.

For example, this week marked the 10th anniversary of the enactment of the STOCK Act. That measure, which President Obama signed into law on April 4, 2012, amended the Ethics in Government Act of 1978 and imposed new financial disclosure requirements, among other provisions.

Overwhelming bipartisan majorities decided then that the existing statutory framework to combat government corruption, improve financial disclosure and transparency, and curb financial conflicts of interest in government had to be strengthened—or, as the Founders might have put it, that more effectual precautions were necessary to keep our public officials virtuous while they continued to hold their public trust.

Accordingly, the STOCK Act enhanced public disclosure requirements by introducing a requirement to report securities transactions throughout the year closer in time to the transactions rather than just the following year on an annual statement.

Among other things, the STOCK Act also affirmed that insider-trading prohibitions apply to Federal officials and clarified that all Federal officials have a duty of confidentiality and trust to the United States and its citizens with respect to material nonpublic information that they derive from their positions.

These were important steps forward. A friend to many of us, the late Chairwoman, Representative Louise Slaughter, was the primary champion of the STOCK Act and worked for years to see it passed into law, and it is fitting that Congress named the law in her honor.

The 10th anniversary of the STOCK Act would, on its own, provide a good opportunity to review how officials have complied with the law and whether there are ways it could be updated.

Unfortunately, there have been examples in all branches of government that further reforms are needed. Consider the following examples, brought to light by government oversight and ethics groups, several of whom are represented here today, in public reporting.

Reporting by the Insider and other publications found that a Member of Congress failed to file the periodic transaction reports required by the STOCK Act on time.

Reporting has also questioned whether Members engaged in improper trading activities or have financial conflicts of interest. In the early weeks of the pandemic, several Senators bought and sold millions of dollars in stock after attending closed-door, confidential briefings with top national security and health experts on the pandemic and the looming economic shutdown. This included selling stocks that would soon take a hit after the stock market plunged and buying stock in industries that received a boom due to the pandemic, such as remote-work technology, telemedicine companies, car companies manufacturing ventilators, and pharmaceutical makers developing vaccines.

The Department of Justice reportedly reviewed the trading activity of several Senators, and, according to the Securities and Exchange Commission, it is still investigating one Senator's trading activities and related conduct.

Also early in the pandemic, the Chief of Staff to then-President Trump sold between a quarter of a million dollars and a half a million dollars in publicly traded securities the same day that President Trump said the economy was doing, quote, "fantastically." The next day, the value of those holdings plummeted.

At the Federal Reserve, multiple senior officials, including presidents of two of the Fed's twelve Reserve Banks, engaged in large financial transactions when the Fed was playing a key role in decisions about the Nation's economy during the pandemic.

Even before the pandemic, though, there were other troubling signs. The wealthiest President and the richest Cabinet in modern history, which included a significant number of billionaires, also exposed how the law's disclosure requirements are out of date and particularly inadequate for the super-rich who become government officials.

In one case, a former Member of the House was investigated by both the Department of Justice and SEC for insider trading and other violations related to his actions in sharing insider information about a failed clinical trial of an Australian biotech company. He ultimately pleaded guilty to conspiracy to commit securities fraud and false statement charges, and he was sentenced to 26 months in prison, but former President Trump pardoned him, and he was released.

One Trump Administration Cabinet Secretary, a billionaire, repeatedly came under criticism from the Office of Government Ethics for failing to abide by his ethics agreement and for repeated errors in his financial disclosure reports—errors significant enough that OGE determined it could not certify his reports. In the meantime, he reportedly made between $53 million and $127 million while heading the Commerce Department. And, as CREW showed, it is possible that he earned even more than that, but we don't really know how much more due to the outdated loopholes in the disclosure laws.

Last month, a Federal judge imposed a penalty of more than $60,000 against a former Trump White House official after finding that she knowingly failed to file a financial disclosure report, as required by law, for more than a year, despite repeated warnings about her obligation to do so.

In the Judicial Branch, as work by good-government groups and reporting by The Wall Street Journal has revealed, there have been widespread problems with financial conflicts of interest and failures by judges to recuse themselves. According to those reports, between 2010 and 2018, more than 130 Federal judges improperly heard hundreds of court cases in which they or their family members held stock in a party to the litigation. Under Federal law, Federal judges are required to recuse themselves from cases in which they or their spouse or minor child have a financial interest in the subject matter or a party.

Plus, the problem could be even worse than that. The judiciary is literally years behind in making judges' financial disclosures publicly available. Only this year will judges' annual financial disclosure filings covering 2019 finally be available. 2020 still won't be ready. By contrast, when a Member of the House files a financial disclosure report, the Clerk must make it publicly available within thirty days.

Across the entire Federal Government, there have been significant and troubling stories about financial conflicts of interest in relation to stock trading and ownership. Together, these stories undermine confidence that the American people should be able to have in the faith and the trust that they put in the integrity of public officials and our government. Members of the public may ask, are our public officials acting in the public interest or their private financial interest?

Considering these events, the Speaker of the House tasked the Committee on House Administration with conducting a comprehensive review of deficiencies in our financial disclosure system and a review of various legislative proposals introduced by Members to address financial conflicts of interest in Congress, including those that aim to restrict stock trading and ownership.

Our hearing today is a continuation of our review of the diverse legislative reform proposals. While there is growing bipartisan consensus that reforms are necessary, there remain significant policy questions about the appropriate approach and the details.

Today, we will have the opportunity to hear from well-respected experts in government ethics and securities law and regulation about what has prompted a significant momentum for financial-conflict-of-interest reforms, the details, variations, implications of various introduced bills, and specific policy recommendations for reform.

It is our hope that this hearing today will bring us closer to developing a consensus on recommended policy reforms that will combat financial conflicts of interest and restore public faith and trust in our government.

Frankly, I have been asked by several reporters, what is the work product that is going to emerge from this hearing? I have been honest to say, we don't know. We have a series of experts who are going to help us understand the intricacies of these issues and will help us in formulating good policy that will buck up trust in the American Government. We do thank the witnesses for their participation.

I would now recognize the Ranking Member—or, did you want to go to Mr. Steil?

Mr. Davis. Only for the questions.

The CHAIRPERSON [continuing] The Ranking Member for any statement he may wish to make.

[The statement of the Chairperson follows:]

One Hundred Seventeenth
Congress of the United States
House of Representatives

COMMITTEE ON HOUSE ADMINISTRATION
1309 LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, DC 20515–6157
202–225–2061 | CHA.HOUSE.GOV

Chairperson Zoe Lofgren
Examining Stock Trading Reforms for Congress
April 7, 2022
Opening Statement

For all of us who are fortunate enough to work in public service, a guiding principle should be the adage that, "A public office is a public trust." Without the public's trust and confidence, government loses its legitimacy. That principle was of paramount importance to the Founders.

As The Federalist Papers put it, "The aim of every political Constitution is or ought to be first to obtain for rulers, men who possess most wisdom to discern, and most virtue to pursue the common good of the society; and in the next place, to take the most effectual precautions for keeping them virtuous, whilst they continue to hold their public trust."

Since the founding, this has remained a vital underpinning of our democracy and informed periodic reforms to address shortcomings in standards of conduct for public officials. For example, this week marked the tenth anniversary of the enactment of the STOCK Act. That measure, which President Barack Obama signed into law on April 4, 2012, amended the Ethics in Government Act of 1978, and imposed new financial disclosure requirements, among other provisions.

Overwhelming bipartisan majorities decided then that the existing statutory framework to combat government corruption, improve financial disclosure and transparency, and curb financial conflicts of interest in government had to be strengthened. Or, as the Founders might have put it, that more "effectual precautions were necessary to keep our public officials virtuous, while they continue to hold their public trust."

Accordingly, the STOCK Act enhanced public disclosure requirements by introducing a requirement to report securities transactions throughout the year, closer in time to the transactions, rather than just the following year, on an annual statement.

Among other things, the STOCK Act also affirmed that insider trading prohibitions apply to federal officials and clarified that all federal officials have a duty of confidentiality and trust to the United States and its citizens with respect to material, non-public information that they derive from their positions.

These were important steps forward. A friend to many of us, the late Chairwoman Louise Slaughter, was the primary champion of the STOCK Act and worked for years to see it passed into law. It's fitting that Congress has named the law in her honor.

The tenth anniversary of the STOCK Act would, on its own, provide a good opportunity to review how officials have complied with the law and whether there are ways it could be updated. Unfortunately, there have been examples in all branches of government that further reforms are needed.

Consider the following examples, brought to light by government oversight and ethics groups – several of whom are represented here today – and public reporting:

- Reporting by *Insider* and other publications found that a number of Members of Congress failed to file the Periodic Transaction Reports required by the STOCK Act on time. Reporting has also questioned whether Members engaged in improper trading activity or have financial conflicts of interest.
- In the early weeks of the pandemic, several Senators bought and sold millions of dollars in stock after attending closed-door, confidential briefings with top national security and health experts on the pandemic and the looming economic shutdown. This included selling stocks that would soon take a hit after the stock market plunged and buying stock in industries that received a boom due to the pandemic, such as in remote-work technology, telemedicine companies, car companies manufacturing ventilators, and pharmaceutical makers developing vaccines. The Department of Justice reportedly reviewed the trading activity of several Senators and, according to the Securities and Exchange Commission, it is still investigating one Senator's trading activity and related conduct.
- Also early in the pandemic, the Chief of Staff to then President Trump sold between a quarter million dollars and a half million dollars in publicly traded securities the same day that President Trump said the economy was doing "fantastically." The next day, the value of those holdings plummeted.
- At the Federal Reserve, multiple senior officials – including presidents of 2 of the Fed's 12 Reserve Banks – engaged in large financial transactions when the Fed was playing a key role in decisions about the nation's economy during the pandemic.

Even before the pandemic, though, there were other troubling signs. The wealthiest President and richest Cabinet in modern history – which included a significant number of billionaires – also exposed how the law's disclosure requirements are out of date, and particularly inadequate for the super-rich who become government officials.

- In one case, a former Member of the House was investigated by both the Department of Justice and the SEC for insider trading and other violations related to his actions in sharing insider information about a failed clinical trial of an Australian biotech company. He ultimately pleaded guilty to conspiracy to commit securities fraud and false statements charges and he was sentenced to 26 months in prison. But former President Trump pardoned him and he was released.
- One Trump Administration Cabinet secretary, a billionaire, repeatedly came under criticism from the Office of Government Ethics for failing to abide by his ethics agreement and for repeated errors in his financial disclosure reports – errors significant enough that OGE determined it could not certify his reports. In the meantime, he reportedly made between $53 million and $127 million while heading the Commerce Department. And as CREW showed, it's possible that he earned even more than that, but we don't really know how much more due to outdated loopholes in the disclosure laws.
- Last month, a federal judge imposed a penalty of more than $60,000 against a former Trump White House official after finding that she knowingly failed to file a financial disclosure report as required by law for more than a year, despite repeated warnings about her obligation to do so.
- In the judicial branch, as work by good government groups and reporting by the *Wall Street Journal* has revealed, there have been widespread problems with financial conflicts of interest and failures by judges to recuse themselves. According to those reports, between 2010 and 2018, more than 130 federal judges improperly heard hundreds of court cases in which they or their family members held stock in a party in the litigation. Under federal law, federal judges are required to recuse themselves from cases in which they or their spouse or minor child have a financial interest in the subject matter or party.
- Plus, the problem could be even worse than that. The judiciary is literally years behind in making judges' financial disclosures publicly available. Only this year will judges' annual financial disclosure filings covering <u>2019</u> finally be available – 2020 <u>still</u> won't be ready. By comparison, when a Member of the House files a financial disclosure report or PTR, the Clerk must make it publicly available within 30 days.

Across the entire federal government, there have been significant and troubling stories about financial conflicts of interest in relation to stock trading and ownership. Together, these stories undermine the American people's faith and trust in the integrity of public officials and our federal government. Members of the public may understandably ask, are our public officials acting in the public interest, or their private financial interest?

In light of these events, the Speaker of the House tasked the Committee on House Administration with conducting a comprehensive review of deficiencies in our financial disclosure system and a review of various legislative proposals introduced by Members to address financial conflicts of interest in Congress, including those that aim to restrict stock trading and ownership.

Our hearing today is a continuation of our review of the diverse legislative reform proposals. While there is growing bipartisan consensus that reforms are necessary, there remain significant policy questions about the appropriate approach and the details. Today, we will have the opportunity to hear from well-respected experts in government ethics and securities law and regulation about what has prompted significant momentum for financial conflicts of interest reform, the details, variations and implications of the various introduced bills, and specific policy recommendations for reform.

It is our hope that this hearing today will bring us closer to developing a consensus on recommended policy reforms that will combat financial conflicts of interest and restore public faith and trust in our government.

I look forward to hearing from our witnesses today.

OPENING STATEMENT OF HON. RODNEY DAVIS, RANKING MEMBER

Mr. DAVIS. Yes, don't give Steil the glory of my opening statement here, Madam Chairperson. First questions, yes, but, I mean, please.

Nice to see you too, Ms. Spanberger. I saw you walk in. Welcome.

Thank you, Chairperson Lofgren. I am glad we are holding a hearing on this very important topic. The public has spoken, and the demand is clear: Americans want more certainty that their elected Representatives are acting in good faith with their financial decisions.

Today provides a unique opportunity to bring together experts from across the political spectrum to assess proposals on how best to move forward to increase transparency and accountability across Congress. I look forward to these discussions, and I am confident this hearing will serve to inform us as we move forward in the legislative process.

I would like to begin by discussing some of the financial transparency measures already in place.

The intent of the 2012 STOCK Act is good. It was meant to create a public disclosure system for Members of Congress to report their trades in a timely manner. However, as we have witnessed on multiple occasions since its passage, the STOCK Act has deficiencies, and compliance with its requirements is not as straightforward for Members as it should be. We have given the STOCK Act ten years, and it is time for Congress to take another look at this issue.

According to Business Insider, at least 59 Members have reportedly violated the requirements of the STOCK Act since 2019. These alleged violators come from both sides of the aisle, making this a bipartisan issue that requires a bipartisan response.

Given the broad distribution of these alleged violations across the various ideological groups in Congress, I am confident that the majority, if not all of them, weren't malicious but inadvertent, illustrating a failure on multiple levels.

This particularly concerns me because it suggests that we are not adequately educating our incoming Members on their responsibilities to comply with the STOCK Act. It is the responsibility of this Committee to ensure Members are aware of their responsibilities when they come to Congress, and I pledge to fix this lapse for new Republican Members. I would ask the Chairperson to join me in this initiative for any incoming Members of her party.

While the legislative fixes we discuss today are a critical step forward, I would like to say also that this Committee should hold further discussions on how best to educate and assist all Members, especially freshman Members, with compliance issues and questions so that we can achieve the transparency that the American people demand.

The public and our Members deserve better from this Committee, and, as Ranking Member, I will do everything I can to fix that. I am sure the Chairperson will agree with this sentiment, and I welcome the opportunity to work together on this bipartisan issue.

Regarding potential STOCK Act updates, I am excited to hear from our witnesses today. Since this issue has captured the attention of the public, we have seen a wide range of proposals for reform. These suggestions are diverse both in their proposed requirements and with their enforcement mechanisms to ensure compliance.

Now, I don't really have many stock holdings other than retirement, but, in anticipation of this hearing, I spoke with my financial advisor from my home district. He is from my home district in Illinois. I wanted to get a better sense of how some of these proposals would affect Members, especially middle-class Members.

He raised the concern that blind trusts, for example, can be cumbersome and expensive, would create perverse incentives, and do not provide the level of transparency that some assume they would. For example, most financial firms won't even take on a client for a blind trust unless they meet certain asset holdings and activity requirements. I don't meet either of those requirements today, and I would guess that is true for many Members. But these cost restrictions would put us in a situation where these perverse incentives might force Members to engage in more market trading to meet blind-trust minimums and other requirements.

I hope we can address some of these concerns here today, because I am sure many Members of Congress share them with me. I am hopeful that the Majority will take this opportunity to work together to build a bipartisan solution instead of proceeding with a knee-jerk reaction that sends a one-party bill immediately to the Floor.

I look forward to our expert witnesses' testimony and further discussion, and I hope we can leave this hearing with a better understanding of the ramifications of any proposed solution as we embark on working together, hopefully, to craft bipartisan legislation.

Thank you. And, with that, I yield back.

[The statement of Mr. Davis follows:]

One Hundred Seventeenth
Congress of the United States
House of Representatives

COMMITTEE ON HOUSE ADMINISTRATION
1309 LONGWORTH HOUSE OFFICE BUILDING
WASHINGTON, DC 20515–6157
202–225–2061 | CHA.HOUSE.GOV

Ranking Member Rodney L. Davis
Examining Stock Trading Reforms for Congress
April 7, 2022
Opening Statement

Thank you, Chairperson Lofgren. I am glad we are holding a hearing on this very important topic. The public has spoken, and the demand is clear: Americans want more certainty that their elected Representatives are acting in good faith with their financial decisions. Today provides a unique opportunity to bring together experts from across the political spectrum to assess proposals on how best to move forward to increase transparency and accountability across Congress. I look forward to these discussions, and I am confident this hearing will serve to inform us as we move forward in the legislative process.

I would like to begin by discussing some of the financial transparency measures already in place. The intent of the 2012 STOCK Act is good. It was meant to create a public disclosure system for Members of Congress to report their trades in a timely manner. However, as we have witnessed on multiple occasions since its passage, the STOCK Act has deficiencies, and compliance with its requirements is not as straightforward for Members as it should be.

According to Business Insider, at least 59 Members have reportedly violated the requirements of the STOCK Act since 2019. These alleged violators come from both sides of the aisle, making this a bipartisan issue that requires a bipartisan response. Given the broad distribution of these alleged violations across the various ideological groups in Congress, I am confident that the Majority, if not all of them, were not malicious but inadvertent, illustrating a failure on multiple levels.

This particularly concerns me because it suggests that we are not adequately educating our incoming Members on their responsibilities to comply with the STOCK Act. It is the responsibility of this Committee to ensure Members are aware of their responsibilities when they come to Congress, and I pledge to fix this lapse for new Republican Members. I would ask the Chairperson to join me in this initiative for any incoming Members of her party.

While the legislative fixes we discuss today are a critical step forward, I would like to say also that this Committee should hold further discussions on how best to educate and assist all Members, especially freshman Members, with compliance issues and questions so that we can achieve the transparency that the American people demand. The public and our Members deserve better from this Committee, and, as Ranking Member, I will do everything I can to fix that. I am sure the Chairperson will agree with this sentiment, and I welcome the opportunity to work together on this bipartisan issue.

Regarding potential STOCK Act updates, I am excited to hear from our witnesses today. Since this issue has captured the attention of the public, we have seen a wide range of proposals for reform. These suggestions are diverse both in their proposed requirements and with their enforcement mechanisms to ensure compliance.

Now, I don't really have many stock holdings other than retirement, but, in anticipation of this hearing, I spoke with my financial advisor from my home district. He is from my home district of Illinois. I wanted to get a better sense of how some of these proposals would affect Members, especially middle-class Members.

He raised the concern that blind trusts, for example, can be cumbersome and expensive, would create perverse incentives, and do not provide the level of transparency that some assume they would. For example, most financial firms won't even take on a client for a blind trust unless they meet certain asset holdings and activity requirements. I don't meet either of those requirements today, and I would assume that is true for many Members. But these costs restrictions would put us in a situation where these perverse incentives might force Members to engage in more market trading in order to meet blind-trust minimums and other requirements.

I hope we can address some of these concerns here today, because I am sure many Members of Congress share them with me. I am hopeful that the Majority will take this opportunity to work together to build a bipartisan solution instead of proceeding with a knee-jerk reaction that sends a one-party bill immediately to the House Floor.

I look forward to our expert witnesses' testimony and further discussion, and I hope we can leave this hearing with a better understanding of the ramifications of any proposed solution as we embark on working together, hopefully, to craft bipartisan legislation. Thank you, Madam Chairperson, and with that, I yield back.

The CHAIRPERSON. Thank you, Mr. Davis.

And in just a moment I will introduce today's witnesses, but before I do, as a reminder to our witnesses, each of you is recognized for five minutes. There is a lighting system and a timer in front of you, and when your time is up, we ask you to try and wrap up.

Your full written statements will be made part of the record and will inform not only this Committee but members of the public.

The record will remain open for at least five days after this hearing for additional material to be submitted, and we may also have additional questions for you. If that is the case, we would ask that you respond to those questions.

Let me introduce each of our witnesses.

Jacob Straus is a Specialist on the Congress at the Congressional Research Service, where he has worked since August 2007. He specializes in American Government and politics, with a focus on Congress and other governmental institutions.

He is an Adjunct Professor on governmental studies at Johns Hopkins University and an Adjunct Professor at the University of Maryland, Baltimore County in the Political Science Department. Prior to that, he served as an Assistant Professor of political science at Frostburg State University.

He holds a Ph.D. in political science from the University of Florida, an M.A. in political science from the University of Florida, and a B.A. in government and politics from the University of Maryland.

Liz Hempowicz serves as Director of Public Policy for the Project on Government Oversight, sometimes referred to as "POGO." She is an expert on whistleblower protections, conflicts of interest, ethics, the Freedom of Information Act, separation of powers, and the National Emergencies Act.

She develops and advances policy solutions to combat corruption and promote openness and accountability in government, and she strategizes the best way to translate POGO report findings to legislative reforms or executive action. She has participated in efforts to improve the Inspector General Act, the National Emergencies Act, lobbying and congressional ethics rules, whistleblower protections, the Freedom of Information Act, and other government accountability issues.

She graduated from the University of Bridgeport with a bachelor's degree in international political economy and diplomacy and earned her J.D. from American University's Washington College of Law.

Donald Sherman, welcome. He serves as the Senior Vice President and Chief Counsel for Citizens for Responsibility and Ethics in Washington, otherwise known as "CREW."

He is a leading policy advisor on racial justice and equity, government ethics, and congressional investigations and oversight. He has served in various roles in the House, Senate, and the Executive Branch, including as Special Assistant to the President for Racial and Economic Justice at the White House, Senior Counsel to Ranking Member Claire McCaskill on the Senate Homeland Security and Governmental Affairs Committee, and Chief Oversight Counsel to the late Representative Elijah Cummings, then-Ranking Member of the House Committee on Oversight and Government Reform.

Mr. Sherman began his career on Capitol Hill as Counsel on the House Ethics Committee when I chaired that committee and where he investigated allegations of ethical violations by Members of Congress and staff. Prior to that, he practiced law in Washington, D.C., for Crowell & Moring LLP and served as a law clerk to the Honorable Neal E. Kravitz of the District of Columbia Superior Court.

He graduated from Georgetown University with a degree in American studies and earned his J.D. from Georgetown University Law Center.

Donna Nagy is the C. Ben Denton Professor of Business Law at Indiana University's Maurer School of Law. She joined the law faculty in 2006 and teaches and writes in securities litigation, securities regulation, and corporations.

Her scholarship includes co-authoring two books, one on the law of insider trading and a casebook on securities litigation and enforcement. She has written numerous Law Review articles on topics including the selective disclosure of government information, government officials and financial conflicts of interest, insider trading, and fiduciary principles.

She is a member of the American Law Institute and served as an appointed member of the ABA Corporate Laws Committee. She also served a three-year term as a member of the National Adjudicatory Council of the Financial Industry Regulatory Authority. Before teaching, she was an associate with Debevoise & Plimpton in Washington, D.C., where she specialized in securities enforcement and litigation.

She received her B.A. from Vassar College and her J.D. from NYU University Law School.

Finally, Jennifer Schulp is the Director of Financial Regulation Studies at the Cato Institute's Center for Monetary and Financial Alternatives, where she focuses on the regulation of securities and capital markets.

Prior to joining Cato, Ms. Schulp was the Director in the Department of Enforcement at the Financial Industry Regulatory Authority, where she represented FINRA investigations and disciplinary proceedings relating to violations of Federal securities laws and self-regulatory organization rules.

Before joining FINRA, Ms. Schulp was a litigation associate at Gibson, Dunn & Crutcher, and she clerked for the Honorable E. Grady Jolly of the U.S. Court of Appeals for the Fifth Circuit. She received her J.D. from the University of Chicago Law School and her A.B. in political science from the University of Chicago.

As all can see, we have a very distinguished panel of witnesses before us. We do thank you.

We will now hear from you for five minutes each, and we will start with you, Mr. Straus.

STATEMENTS OF JACOB STRAUS, SPECIALIST ON CONGRESS, CONGRESSIONAL RESEARCH SERVICE, WASHINGTON, D.C.; LIZ HEMPOWICZ, DIRECTOR OF PUBLIC POLICY, PROJECT ON GOVERNMENT OVERSIGHT, WASHINGTON, D.C.; DONALD SHERMAN, SENIOR VICE PRESIDENT AND CHIEF COUNSEL, CITIZENS FOR RESPONSIBILITY AND ETHICS IN WASHINGTON; DONNA NAGY, C. BEN DUTTON PROFESSOR OF BUSINESS LAW, INDIANA UNIVERSITY MAURER SCHOOL OF LAW, BLOOMINGTON, INDIANA; AND JENNIFER J. SCHULP, DIRECTOR OF FINANCIAL REGULATION STUDIES, CATO INSTITUTE, WASHINGTON, D.C.

STATEMENT OF JACOB STRAUS

Mr. STRAUS. Chairperson Lofgren, Ranking Member Davis, and Members of the Committee, on behalf of the Congressional Research Service, thank you for the opportunity to appear today.

My testimony focuses on two areas: current financial disclosure and periodic transaction reporting requirements; and legislative proposals introduced during the 117th Congress to limit or prohibit certain financial transactions by Members of Congress and covered congressional employees.

Federal Government officials and employees, including Members of Congress, when taking official action, are expected to, quote, "place loyalty to the Constitution, laws, and ethical principles above private gain."

Using this guiding principle, the Ethics in Government Act, as amended, including by the STOCK Act in 2012, requires covered officials, including Members of Congress and certain congressional employees, to file annual financial disclosure statements that report income, gifts, liabilities, and property and make periodic transaction reports that disclose the purchase or sale of certain financial assets.

Further, the STOCK Act affirms that Members of Congress, congressional employees, and other Federal officials are not exempt from insider-trading laws.

In the 117th Congress, as of March 1, 2022, CRS identified fourteen bills or resolutions that proposed limitations on Members of Congress and other covered congressional employees from engaging in certain financial transactions. Broadly, these measures propose to amend the Ethics in Government Act and/or the STOCK Act, create new law, or amend House rules to prohibit the holding, purchasing, selling, and or actively managing certain types of assets.

Currently, Congress does not prohibit the ownership of specified financial assets, but certain targeted restrictions do exist in some Executive Branch agencies.

With regard to the legislative proposals before Congress, six points are pertinent.

First, to address Member and covered individuals' financial holdings and transactions, several legislative proposals would either amend the Ethics in Government Act, the STOCK Act, or both. Others would create new law.

Second, each of the legislative proposals would generally prohibit covered officials from holding, purchasing, selling, and/or actively managing certain types of assets.

Third, a number of the proposals would allow or require a Member of Congress to place covered assets in a qualified blind trust that is approved by the official's supervising ethics office, the House Ethics Committee for the House of Representatives. Qualified blind trusts separate the covered official from day-to-day decisionmaking about their holdings, which could serve to remedy potential conflicts that might arise from officials' actions that could impact their individual holdings.

Fourth, four of the proposals would expand public access to information in the financial disclosure statements and periodic transaction reports.

Fifth, ten of the fourteen legislative proposals would change available penalties for noncompliance. Within these proposals, two basic penalty strategies are suggested: fine individuals for noncompliance and/or publish the names of individuals who are found in violation of the law on a public web page.

Finally, two legislative proposals would amend House Rule XXIII, the House Code of Conduct, to add a new section that would prohibit Members from trading stocks.

In closing, these legislative proposals include a range of options to limit or prohibit certain financial activities. Policymakers may wish to consider the scope of these proposals, the benefits of proposals, any potential administrative adjustments that might be necessary to implement a modification of ethics laws, and the potential costs to covered officials to comply with the proposed laws. My written testimony raises questions that might be considered.

Should Congress choose to act, it could implement a particular measure as introduced or incorporate various concepts from several different measures. Each choice likely has advantages and disadvantages that CRS is available to discuss further.

Thank you again for the opportunity to testify. I look forward to your questions.

[The statement of Mr. Straus follows:]

Congressional Research Service
Informing the legislative debate since 1914

TESTIMONY

Statement of

Jacob R. Straus
Specialist on the Congress

Before

Committee on House Administration
U.S. House of Representatives

Hearing on

"Examining Stock Trading Reforms For Congress"

March 16, 2022

Congressional Research Service
7-5700
www.crs.gov
<Product Code>

Chairperson Lofgren, Ranking Member Davis, and Members of the Committee, on behalf of the Congressional Research Service thank you for this opportunity to discuss current legislative proposals that would limit or prohibit certain financial transactions by Members of Congress.

My testimony focuses on three areas: (1) current financial disclosure laws under the Ethics in Government Act; (2) current disclosure requirements for financial transactions under the STOCK Act; and (3) an analysis of current legislative proposals to limit or prohibit certain financial transactions introduced in the 117th Congress (2021-2022). The discussion of current legislative proposals focuses on the content of the bills and resolutions, including proposed prohibitions on holding, purchasing, and/or selling certain assets; amendments to the Ethics in Government Act and/or STOCK Act; potential requirements for the use of qualified blind trusts; changes to public access of disclosure documents; and proposed penalties for non-compliance. Additionally, this testimony discusses two proposals to amend House Rule XXIII, the Code of Conduct.

This written statement is drawn largely from other CRS products, including CRS Insight 11860, *Stock Trading in Congress: 117th Congress Proposals to Limit or Prohibit Certain Financial Transactions*. Accordingly, my statement summarizes and expands key portions of the Insight, and addresses the legislative proposals introduced to date in the 117th Congress.

Background on Current Financial Disclosure Laws

Federal government officials and employees, including Members of Congress, when taking official action, are expected to "put loyalty to the highest moral principles and to country above loyalty to persons, party, or Government department."[1] Using these guiding principles, in 1978, Congress enacted the Ethics in Government Act, which created the current government ethics program to "preserve and promote the integrity of public officials and institutions."[2]

As amended,[3] the Ethics in Government Act requires covered employees, including Members of Congress, congressional officers, and selected congressional staff,[4] to file annual financial disclosure

[1] Code of Ethics for Government Service (H.Con.Res. 975 (1958), 72 Stat. B12). The standards included in the Code of Ethics for Government Service are still recognized as continuing ethics guidance in the House and Senate. They are not legally binding, because the code was adopted by congressional resolution, not by public law. The Code of Ethics for Government Service is cited by many House and Senate investigations. For example, see U.S. Congress, House Committee on Standards of Official Conduct, *Investigation of Certain Allegations Related to Voting on the Medicare Prescription Drug, Improvement, and Modernization Act of 2003*, report, 108th Congress, 2nd sess., H.Rept. 108-722 (Washington: GPO, 2004), p. 38. See also 5 C.F.R. §2635.101(a), which applies to executive branch employees, and 18 U.S.C. §208, which prohibits executive branch employees from participating "personally and substantially" in any covered activity in which the employee or the employee's spouse, minor child, general partner, or previous organization has a financial interest.

[2] P.L. 95-521, 92 Stat. 1824 (1978); 5 U.S.C. Appendix §§101-112.

[3] P.L. 101-194, 103 Stat. 1724 (1989); P.L. 112-105, 126 Stat. 291 (2012); 5 U.S.C. Appendix §§101-112.

[4] The House *Ethics Manual* defines financial disclosure filers as "all Members of the House and those House employees earning —above GS-15, that is, at least 120% of the federal GS-15 base level salary, for at least 60 days during the calendar year must file a Financial Disclosure Statement by May 15 of each year." U.S. Congress, House Committee on Standards of Official Conduct, *House Ethics Manual*, "Who Must File," 110th Cong., 2nd sess. (Washington: GPO, 2008), p. 252. For CY 2022, "the GS-15, step 1, basic pay rate ... is $112,890. The applicable 120% calculation for that rate is therefore $135,468, or a monthly salary of equal to or more than $11,289. This rate is referred to as the "senior staff rate." U.S. Congress, House, Committee on Ethics, "The 2022 Outside Earned Income Limit and Salaries Triggering the Financial Disclosure Requirement and Post-Employment Restrictions Applicable to House Officers and Employees," *Pink Sheet*, January 13, 2022, p. 2, at https://ethics.house.gov/sites/ethics.house.gov/files/documents/Final%202022%20Annual%20Pay%20Memo%2001132022.pdf. The Senate uses the same definition for filers. See U.S. Congress, Senate, Select Committee on Ethics, "Chapter 5: Financial Disclosure," *Senate Ethics Manual, 2003 edition*, p. 125, at https://www.ethics.senate.gov/public/index.cfm/files/serve?File_id=f2eb14e3-1123-48eb-9334-8c4717102a6e.pdf#page=137.

statements that report "income, gifts, liabilities, property—both real property and business-related personal property—positions in business enterprises and other organizations and also any agreements relating to post-Government employment."[5] As one scholar noted, "the Ethics in Government Act of 1978 [is] a reflection of one of our nation's most fundamental aspirations for government: that official decisions should be made in the interests of the common good, not in the narrow self-interests of the individuals in power."[6]

Members of Congress and officers or employees of the Congress are included as covered officials in the Ethics in Government Act.[7] Subsequent amendments provided that Representatives, Delegates, the Resident Commissioner, Senators, House and Senate officers, and other specified covered employees are required to file annual financial disclosures statements with the Clerk of the House of Representatives and the House Ethics Committee,[8] or the Secretary of the Senate and Senate Select Committee on Ethics,[9] respectively. The House Ethics Committee and the Senate Select Committee on Ethics each provide guidance for financial disclosure filing.[10]

Stock Trading Disclosure in Congress

On April 4, 2012, President Obama signed the STOCK Act.[11] The STOCK Act, as amended, affirms that Members of Congress, congressional employees, and other federal officials are not exempt from "insider trading"[12] laws and regulations.[13] It also requires covered individuals (primarily those that already file financial disclosure statements) to file periodic transaction reports with their supervising ethics office within 30 days of receiving notification of a covered financial transaction and no later than 45 days after

---

[5] U.S. Congress, House Committee on the Judiciary, *Ethics in Government Act of 1977*, report to accompany H.R. 1, 95th Cong., 1st sess., November 2, 1977, H.Rept. 95-800 (Washington: GPO, 1977), p. 16.

[6] Beth Nolan, "Removing Conflicts from the Administration of Justice: Conflicts of Interest and Independent Counsels Under the Ethics in Government Act," *Georgetown Law Journal*, vol. 79, no. 1 (October 1990), p. 2.

[7] 5 U.S.C. Appendix §101(f)(9)-(10). For further clarification on the definition of Members of Congress and officers or employees of the Congress, definitions, see 5 U.S.C. Appendix §109(12)-(13).

[8] U.S. Congress, House, Office of the Clerk of the House of Representatives, *Financial Disclosure Reports*, at https://disclosures-clerk.house.gov/PublicDisclosure/FinancialDisclosure; and U.S. Congress, House, Committee on Ethics, "Financial Disclosure," at https://ethics.house.gov/financial-disclosure.

[9] Senate Rule XXXIV. U.S. Congress, Senate, Secretary of the Senate, "Senate Public Financial Disclosure (Senate Rule 34), *Public Disclosure*, at https://www.senate.gov/pagelayout/legislative/g_three_sections_with_teasers/lobbyingdisc.htm; and U.S. Congress, Senate, Select Committee on Ethics, "Financial Disclosure," at https://www.ethics.senate.gov/public/index.cfm/financialdisclosure.

[10] U.S. Congress, House, Committee on Ethics, "Financial Disclosure Guidance," at https://ethics.house.gov/forms/fd-guidance; and U.S. Congress, Senate, Select Committee on Ethics, "Chapter 5: Financial Disclosure," *Senate Ethics Manual, 2003 edition*, at https://www.ethics.senate.gov/public/index.cfm/files/serve?File_id=f2eb14e3-1123-48eb-9334-8c4717102a6e.pdf#page=135.

[11] P.L. 112-105, 126 Stat. 291 (2012). The STOCK Act was renamed the Representative Louise McIntosh Slaughter Stop Trading on Congressional Knowledge Act by P.L. 115-277 (132 Stat. 4167 (2018)).

[12] For more information on insider trading, see CRS InFocus IF11966, *Insider Trading*, by Jay B. Sykes.

[13] The STOCK Act (P.L. 112-105, §13) also prohibits Members, officers, and employees who file financial disclosure statements from participating in Initial Public Offerings (IPOs). In a February 2019 memorandum to House Members, officers, and employees, the House Ethics Committee noted that "while interpretation and enforcement of the STOCK Act regarding participation in IPOs is chiefly within the jurisdiction of the SEC and Department of Justice, the opinion of the Committee is that, as drafted, the STOCK Act prohibits only the filer from participating in IPOs, but not the filer's spouse or dependent child, assuming the assets used for the purchase and the securities purchased are wholly owned by the spouse or dependent child, separate and independent of the filer." See U.S. Congress, House Committee on Ethics, *Summary of Activities One Hundred Sixteenth Congress*, 116th Cong., 2nd sess., December 31, 2020, H.Rept. 116-703 (Washington: GPO, 2020), p. 47, note 18. [Hereinafter House Ethics Committee, *Summary of Activities*, 116th Congress]

the transaction.[14] For the House of Representatives, the supervising ethics office is the House Ethics Committee, and for the Senate it is the Senate Select Committee on Ethics.[15]

Under STOCK Act amendments to the Ethics in Government Act, covered individuals, including Members of Congress, officers, and covered congressional employees report financial transactions (e.g., sales and purchases of stocks, bonds, commodity futures, and other securities) that exceeded $1,000.[16] Periodic transaction reports are filed in the same manner as the covered official's annual financial disclosure. For Members of Congress, both their financial disclosure forms and their periodic transactions reports are available for public inspection from the Clerk of the House (for Representatives) or the Secretary of the Senate (for Senators).[17]

Proposals to Limit or Prohibit Certain Financial Transactions in the 117th Congress

In the 117th Congress, there has been interest in further limiting or prohibiting Members of Congress and other covered congressional officials and employees from engaging in certain financial transactions. As of March 1, 2022, some Members of Congress have introduced at least 14 bills or resolutions on these issues, eight in the House and six in the Senate. Broadly, these measures propose to amend the Ethics in Government Act, the STOCK Act, and/or House Rules to prohibit certain transactions, increase financial disclosure reporting requirements, and prescribe remedies to alleviate real or perceived conflicts of interest and penalties for engaging in certain behaviors. **Table 1** lists the 14 measures (bill or resolution number and title); the proposed affected party; proposed actions; timeline for implementation, if enacted; and proposed penalties. For organizational ease, **Table 1** lists companion measures together.

[14] Covered filers are required by the Ethics in Government Act to "report on their annual FD Statement each purchase, sale, or exchange transaction involving real property held for investment, stocks, bonds, commodities futures, or other securities (including cryptocurrencies and options) made by the filer, their spouse, or dependent child when the amount of the transaction exceeds $1,000. For sales transactions, the $1,000 threshold is based on the total dollar value of the transaction, not the gain or loss made on the sale. See House Ethics Committee, *Summary of Activities*, 116th Congress, p. 44.

[15] 5 U.S.C. Appendix §103(j).

[16] P.L. 112-105, §6(a). For more information, see U.S. Congress, House, Committee on Ethics, "Reminder of STOCK Act Requirements, Prohibition Against Insider Trading & New Certification Requirements," June 11, 2020, at https://ethics.house.gov/sites/ethics.house.gov/files/wysiwyg_uploaded/STOCK%20Act%206.11.2020%20Final.pdf; and U.S. Congress, Senate, Select Committee on Ethics, "STOCK Act Requirements for Senate Staff," June 15, 2012, at https://www.ethics.senate.gov/public/_cache/files/e63d0a27-19b2-4bf3-b26e-9073ff179e3e/stock-act-requirements-for-senate-staff-1-.pdf.

[17] 5 U.S.C. Appendix §105. For Representatives and Senators, periodic transaction reports and financial disclosure reports, are available for public inspection on the Clerk of the House's and Secretary of the Senate's website, respectively. Periodic transaction reports and financial disclosure reports for officers and other covered congressional employees are not available for public inspection (P.L. 113-7, §1(a)(1), 127 Stat. 438 (2013)). For access to filings, see U.S. Congress, House, Office of the Clerk of the House of Representatives, *Financial Disclosure Reports*, at https://disclosures-clerk.house.gov/PublicDisclosure/FinancialDisclosure; and U.S. Congress, Senate, Secretary of the Senate, "Senate Public Financial Disclosure (Senate Rule 34)," *Public Disclosure*, at https://www.senate.gov/pagelayout/legislative/g_three_sections_with_teasers/lobbyingdisc.htm.

Table 1. Proposals to Limit or Prohibit Certain Financial Transactions, 117th Congress

Through March 1, 2022

Bill or Resolution	Affected Congressional Party	Proposed Action	Timeline	Proposed Penalty
H.Res. 873 No Option for Stock Trading and Ownership as a Check to Keep Congress Clean Resolution	Members of Congress, Delegates, and Resident Commissioner	Amends House Rule XXIII to prohibit ownership of common stock	Not specified	Not specified
H.R. 459 HUMBLE Act	Members of Congress, Delegates, and Resident Commissioner	Amends House Rule XXIII to prohibit ownership of common stock	Effective immediately before noon on January 3, 2023	Not specified
H.R. 336 TRUST in Congress Act	Members of Congress, spouses, and dependent children	Require placement of covered investments in a qualified blind trust; Clerk of the House and Secretary of the Senate post certifications on a public website	Within 90 days of enactment for current Members or within 90 days of taking office for new Members	Not specified
H.R. 1579 Ban Conflicted Trading Act S. 564 Ban Conflicted Trading Act	Members of Congress and congressional employees who file Financial Disclosure reports under the Ethics in Government Act	Prohibits purchase or sale of covered investments; covered officials may place securities holdings in qualified blind trust	Not specified	Civil penalty of not less than 10 percent of the value of the covered investment that was purchased or sold or the security in which a net short position was created in violation of this Act
H.R. 6490 Banning Insider Trading in Congress Act S. 3504 Banning Insider Trading in Congress Act	Members of Congress and spouses	Amend the Ethics in Government Act to prohibit holding, purchase, or sale of covered financial instruments; covered officials may place holdings in qualified blind trust; supervising ethics committee publishes certification on a public website	Within 180 days of enactment for current Members or within 180 days of taking office for new Members	Disgorge to the Treasury any profit from the transaction or holding; prohibition on deduction of a loss from a covered transaction or holding; and civil fine assessed by supervising ethics committee

Bill or Resolution	Affected Congressional Party	Proposed Action	Timeline	Proposed Penalty
H.R. 6694 STOCK Act 2.0 S. 3612 STOCK Act 2.0	Members of Congress, senior congressional staff, spouses, and dependents	Amend Ethics in Government Act to prohibit purchase or sale of covered financial instruments; covered officials may place securities holdings in qualified blind trust; and amend the STOCK Act to require public access to covered officials' financial disclosure and periodic transaction reports	Not specified	Fine pursuant to regulations issued by the supervising ethics office of $500 in each case the covered person fails to file a report Amends STOCK Act to create fines for failure to report ($500 for each case), and requires deposit of fines in the Treasury Civil penalty of not less than 10 percent of the value of the covered investment that was purchased or sold, or the security in which a net short position was created
H.R. 6678 Bipartisan Ban on Congressional Stock Ownership Act of 2022 S. 3631 Bipartisan Ban on Congressional Stock Ownership Act of 2022	Members of Congress and spouses	Prohibit ownership of specified assets and requires divestment of assets except for widely held investment fund	Depending on type of asset, divest within 180 days or 5 years of enactment for current Members or within 180 days or 5 years of taking office for new Members	Civil fines of not more than $50,000 if determined by a United States district court after the Attorney General or Special Counsel brings a civil action
H.R. 6844 Restoring Trust in Public Service Act	Members of Congress, spouses, and dependents	Prohibit ownership of specified assets and requires divestment of covered instruments	Divestment within 90 days of enactment for current Members or within 90 days of taking office for new Members	Penalty equal to the Member's entire federal salary, for as long as the violation continues Publication by the Ethics Committee of individuals found to be in violation

Bill or Resolution	Affected Congressional Party	Proposed Action	Timeline	Proposed Penalty
S. 3494 Ban Congressional Stock Trading Act	Members of Congress, spouses, and dependents	Amend the Ethics in Government Act to require the divestment or placement of covered investments in a qualified blind trust; supervising ethics office makes public qualified blind trust certifications, trust agreement, schedule of assets placed in trust, and descriptions of extensions or penalties	Submit certification within 30 days of enactment for current Members or within 30 days of taking office for new Members Divest or place covered instruments in a qualified blind trust within 120 days of enactment or within 120 days of taking office for new Members	Written notice by supervising ethics office to Member with warning of potential violation to correct actions Civil penalty equal to the monthly equivalent of the annual rate of pay payable to the Member of Congress, if filings are not corrected after the supervising ethics office gives 30 days' notice of noncompliance
S. 3550 Ethics Reform Act	Members of Congress	Prohibit purchase or sale of individual securities	Not specified	Not specified

Source: CRS summary and analysis of proposed legislation.

Notes: To compile this list, CRS searched Congress.gov using subject headers "Government Ethics" + "Members of Congress" + "Securities." CRS supplemented this search by examining House dear colleague letters and Member press releases for similar legislation. It is possible that other measures that might address similar policy matters but use different wording were not captured by this search. Jennifer Manning, Senior Research Librarian, conducted the search on February 14, 2022, and February 28, 2022.

Generally, the 14 measures in **Table 1** propose to regulate the financial activities of Members of Congress and covered congressional staff.[18] Most frequently, these proposals seek to prohibit covered individuals from the holding, purchase, sale, and/or active management of certain types of financial assets; require certain assets to be placed in qualified blind trusts; and/or change access to filings and/or penalties for noncompliance. To accomplish these goals, the legislative proposals seek to amend the Ethics in Government Act and/or the STOCK Act, create new law, or amend House Rules.

Amend Ethics in Government Act, the STOCK Act, and/or Create New Law

Several legislative proposals would either amend the Ethics in Government Act, the STOCK Act, or both.[19] Others would create new law to address Member and covered officials' financial holdings and

[18] Several measures also propose to limit or prohibit particular executive branch officials or federal judges from holding, purchasing, and selling certain assets. For example, H.R. 6694 and S. 3612 "STOCK Act 2.0" both would prohibit the President, the Vice President, the Chief Justice of the United States, Associate Justices of the Supreme Court, members of the Board of Governors of the Federal Reserve System, and presidents and vice presidents of Federal Reserve Banks from engaging in certain transactions. H.R. 6684 would also propose to prohibit stock ownership by executive branch officials (President, Vice President, political appointees, and certain senior career employees) and federal judges.

[19] H.R. 6490, H.R. 6694, S. 3494, S. 3504, and S. 3612.

transactions. In some cases, the proposals would authorize or require the use of a qualified blind trust (see "Require the Use of Qualified Blind Trusts" below) to avoid or prevent potential conflicts of interest.

The legislative proposals to amend the Ethics in Government Act and/or the STOCK Act all focus on codifying new prohibitions on covered individuals from holding, purchasing, or selling covered assets (discussed below under "Prohibit Holding, Purchasing, and Selling Certain Assets"). All of the proposals would apply restrictions to Members of Congress, but some would also apply to Members' spouses and dependents.[20] Fewer would also apply to congressional officers or covered staff members.[21]

While the general approaches of each measure are similar, some differences exist. For example, H.R. 6490 and S. 3504, "The Ethics Reform Act," propose to require that Members of Congress file annual "certification of compliance" forms with their supervising ethics committee, which the committee would then publish on a publicly available website.[22] Further, these measures would authorize the House Ethics Committee and the Senate Select Committee on Ethics to issue civil fines, as they deem appropriate, for non-compliance.[23]

Similarly, H.R. 6694 and S. 3612, "STOCK Act 2.0," propose to authorize the use of qualified blind trusts on a case-by-case basis and establish a civil penalty of "not less than 10 percent of the value of the covered instrument" for a covered individual who knowingly fails to comply with the amendments.[24] Further, the legislation would amend the STOCK Act to require that certain financial disclosure forms be publicly available for Members of Congress and other government officials.[25]

Two other proposals (H.R. 6490 and S. 3504, "Banning Insider Trading in Congress Act") would provide the supervising ethics office with the power to impose civil fines and require the Government Accountability Office (GAO) to audit compliance with the law. GAO has similar authority under the Lobbying Disclosure Act (LDA),[26] which requires GAO to audit LDA filings and submit an annual report to Congress.[27]

---

[20] H.R. 336, H.R. 6490, S. 3504, H.R. 6694, S. 3612, H.R. 6678, S. 3631, H.R. 6844, and S. 3494.

[21] H.R. 1579, S. 564, H.R. 6694, and S. 3612.

[22] H.R. 6490 and S. 3504, §2, proposed new section 203 of the Ethics in Government Act.

[23] H.R. 6490 and S. 3504, §2, proposed new section 204 of the Ethics in Government Act.

[24] H.R. 6694 and S. 3612, §5, proposed new section 205 of the Ethics in Government Act.

[25] H.R. 6694 and S. 3612, §6. Other government officials specified in the legislation include the President, Vice President, presidentially nominated Senate confirmed officials listed in 5 U.S.C. 5312 and 5313; judicial officers; and Officers of Federal Reserve Banks. Currently, financial disclosure statements for the named executive branch officials are available directly from the Office of Government Ethics (OGE) on its "Officials' Individual Disclosure Search Collection" webpage, at https://www.oge.gov/web/oge.nsf/Officials%20Individual%20Disclosures%20Search%20Collection?OpenForm. On February 18, 2022, the Federal Reserve Board of Governors announced new ethics and disclosure rules for the Federal Open Market Committee and Federal Reserve Bank presidents and vice-presidents. For more information, see Board of Governors of the Federal Reserve System, "FOMC Formally Adopts Comprehensive New Rules for Investment and Trading," press release, February 18, 2022, https://www.federalreserve.gov/newsevents/pressreleases/monetary20220218a.htm; and Board of Governors of the Federal Reserve System, "Program for Security of FOMC Information," approved February 17, 2022, with amendments effective May 1, 2022, at https://www.federalreserve.gov/monetarypolicy/files/FOMC_InformationSecurityProgram.pdf.

[26] 2 U.S.C. §§1601-1614. For more information, see CRS Report R44292, *The Lobbying Disclosure Act at 20: Analysis and Issues for Congress*, by Jacob R. Straus.

[27] Under the Lobbying Disclosure Act (LDA; 2 U.S.C. §1614), the Comptroller General is required to conduct an annual audit on "the extent of compliance or noncompliance with the requirements of this chapter by lobbyists, lobbying firms, and registrants through a random sampling of publicly available lobbying registrations and reports filed ... during each calendar year." The most recent report was compiled in April 2021. U.S. Government Accountability Office, *2020 Lobbying Disclosure: Observations on Lobbyists' Compliance with Disclosure Requirements*, GAO-21-375, April 1, 2021, https://www.gao.gov/products/gao-21-375.

Prohibit Holding, Purchasing, and Selling Certain Assets

Each of the legislative proposals in **Table 2** would generally prohibit covered officials from holding, purchasing, selling, and/or actively managing certain types of assets. Aspects of these measures would prohibit the purchase or sale of specified financial instruments, require additional disclosure and potential divestment of prohibited assets, and/or increase penalties for noncompliance. Each measure generally approaches covered assets in a particular way. **Table 2** reports the types of assets covered by each proposal.

Table 2. Covered Assets in Certain Legislative Proposals to Prohibit Holding, Purchasing or Selling Certain Financial Instruments

Legislative Proposal	Covered Assets	Exempted Assets
H.R. 1579/S. 564	Commodities, securities, futures, and any comparable economic interest acquired through synthetic means such as the use of a derivative	Widely held investments; United States Treasury bills, notes, or bonds
H.R. 6490/S. 3504	Security, security future, commodity, and "any [comparable] economic interest ... that is acquired through synthetic means, such as the use of a derivative, including an option, warrant, or other similar means"	Diversified mutual fund, diversified exchange-traded fund, United States Treasury bill, note, or bond; or compensation from the primary occupation of a Members' spouse or dependent
H.R. 6694/S. 3612	Commodity, securities, futures, cryptocurrency, and any comparable economic interest acquired through synthetic means such as the use of a derivative	Widely held investments; United States Treasury bills, notes, or bonds
H.R. 6678/S. 3631	Stock, bond, commodity, future, or "other form of security, including an interest in a hedge fund, a derivative, option, or other complex investment vehicle"	Widely held investments, shares of Settlement Common Stock issued under the Alaska Native Claims Settlement Act (43 U.S.C. §1606(g)(1)(A)); United States Treasury bills, notes, or bonds; investment fund held by federal, state, or local government employee retirement plans; small business concern interests; and compensation from the primary occupation of a spouse
H.R. 6684	Individual stocks, securities, commodities, futures, and derivatives	Diversified mutual funds and environmental, social, and governance (ESG) mutual funds
S. 3550	Individual securities	Widely held investments
H.Res. 873	Common stock of any individual public corporation	None specified
H.R. 459	Common stock of any individual public corporation	None specified

Source: CRS analysis of proposed legislation.

Most of the proposals prohibit Members of Congress from holding, purchasing, or selling similar assets, including commodities,[28] securities,[29] security futures,[30] and other named assets. Currently, Congress does not prohibit the ownership of specified financial assets, but some executive branch agencies do. For example, the Nuclear Regulatory Commission has supplemental Standards of Ethical Conduct that include a list of prohibited securities.[31]

All but two proposals would exempt some type of assets. Most commonly, exemptions include United States Treasury bills, notes, or bonds; and certain "widely held investments."[32] Widely held investments would generally not need to be reported, but must meet three criteria: the fund must be publicly traded, the assets of the fund are widely diversified, and "the reporting individual neither exercises control over nor has the ability to exercise control over the financial interests held by the fund."[33]

Require the Use of Qualified Blind Trusts

A number of the proposals would allow or require a Member of Congress (and their spouses and/or dependent children) to place covered assets in a qualified blind trust.[34] Qualified blind trusts are specific instruments that may be used to remediate real or perceived financial conflicts of interest.[35] Created in the Ethics in Government Act, qualified blind trusts

> confer on an independent trustee and any other designated fiduciary the sole responsibility to administer the trust and to manage trust assets without participation by, or the knowledge of, any interested party or any representative of an interested party. This responsibility includes the duty to decide when and to what extent the original assets of the trust are to be sold or disposed of, and in what investments the proceeds of sale are to be reinvested.[36]

The establishment of a qualified blind trust requires permission from a covered official's supervising ethics office (e.g., the House Committee on Ethics or the Senate Select Committee on Ethics for Representatives and Senators, respectively). Should a qualified blind trust be established to remediate a financial conflict of interest, the covered official "gives up the management of the assets to an independent trustee, who makes investment decisions of the individual's benefit without the individual's knowledge."[37] Further, the trustee must

---

[28] Generally defined in section 1a of the Commodity Exchange Act; 7 U.S.C. §1a.

[29] Generally defined in section 3(a) of the Securities Exchange Act of 1934; 15 U.S.C. §78c(a).

[30] Ibid.

[31] 5 C.F.R. §5801.102(b).

[32] The Office of Government Ethics (OGE) notes, "an investment fund is widely held if the fund has at least 100 natural persons as direct or indirect investors. For example, if a pension plan invests in the ABC Fund, one would count each plan participant toward the 100-person threshold when determining whether the ABC Fund is widely held." See U.S. Office of Government Ethics, *Confidential Financial Disclosure Guide: OGE Form 450*, December 2018, p. 32, at https://www.oge.gov/Web/OGE.nsf/0/A685AEC70F057115852585B6005A202F/$FILE/Confidential%20Fin%20Disc%20Guide_Jan2019.pdf#page=32. Similar guidance exists in OGE's *Public Financial Disclosure Guide*, p. 290, at https://www.oge.gov/Web/OGE.nsf/0/11E9ABAF6E128FF1852585B6005A2030/$FILE/Public%20Fin%20Disc%20Guide_Jan2019.pdf#page=290.

[33] 5 U.S.C. Appendix §102(f)(8).

[34] H.R. 336, H.R. 6844, S. 3494, H.R. 1579 and S. 564, and H.R. 6694 and S. 3612.

[35] 5 C.F.R. §2634.401.

[36] 5 C.F.R. §2634.401(a).

[37] U.S. Congress, Senate Select Committee on Ethics, *Qualified Blind Trusts*, 114th Cong., 1st sess., September 2015, p. 1, at https://www.ethics.senate.gov/public/_cache/files/286a4cf9-5aab-40ef-9a6c-bf2278e79e38/qualified-blind-trusts-guide---october-2020.pdf. [Hereinafter *Qualified Blind Trusts*]

> be an independent financial institution, lawyer, certified public accountant, broker, or investment advisor; there may be no restrictions on the disposal of the trust assets; [and] the trust instrument must limit communications between the trustee and interested parties.[38]

Qualified blind trusts may be considered expensive to establish and maintain.[39] Accordingly, some supervising ethics offices have determined that they are not always an appropriate remedy when other solutions might be available.[40]

At least two proposals (H.R. 336 and S. 3494) would require a covered official to either divest or place certain assets in a qualified blind trust. Current Members of Congress would be required to divest and/or place covered assets in a qualified blind trust within a specified number of days of enactment. New Members of Congress would have to do the same within a specified number of days after being sworn in.[41] Other proposals would provide the option of using a qualified blind trust.[42]

Qualified blind trusts can serve as a way to "immunize" a public official "from potential conflicts of interest stemming from assets held in the trust because the legislator-beneficiary would have no knowledge of the impact of official actions on [their] personal financial interests."[43] If a covered official places their assets in a qualified blind trust they are separated from the day-to-day decision making about their holdings, which can serve to remedy potential conflicts that might arise from decision-making that could impact their individual holdings.

The creation of a significant number of new qualified blind trusts could present administrative challenges to the House and Senate. In a scenario where all Representatives, delegates, and the Resident Commissioner, and Senators, were required to create a qualified blind trust within a certain number of days of enactment, the review and certification process currently used by the House Ethics Committee and the Senate Select Committee on Ethics could be strained. A similar scenario, albeit with a smaller number of individuals, could occur at the beginning of each subsequent Congress, as newly elected Members would have a deadline by which they would need to seek approval of their trust documents. Should Congress enact a proposal to require the use of qualified blind trust, the House Committee on Ethics and the Senate Select Committee on Ethics might require additional resources to conduct necessary reviews and certifications.

The House and Senate do not currently appear to publish data on the number of qualified blind trusts reviewed or certified. The House Ethics Committee and the Senate Select Committee on Ethics, however, do report the total number of financial disclosure and periodic transaction reports that it receives annually.

---

[38] U.S. Congress, House Committee on Ethics, "Trusts," *Specific Disclosure Requirements*, at https://ethics.house.gov/financial-dislosure/specific-disclosure-requirements.

[39] *Qualified Blind Trusts*, p. 2. See also, National Conference of State Legislators, "Blind Trusts," at https://www.ncsl.org/research/ethics/blind-trusts.aspx.

[40] *Qualified Blind Trusts*, p. 2. For a discussion of financial conflict of interest remedies, including disqualification (recusal), divestiture, waivers, trusts, and reassignment or resignation, see CRS InFocus 11904, *Financial Disclosure: Identifying and Remediating Conflicts of Interest in the Executive Branch*, by Jacob R. Straus. Similar, but not necessarily the same, remediation options are available in the House and Senate, depending on the filer's role within Congress. Additionally, in some cases, the supervising ethics office can determine that "the financial interest may be deemed too remote or inconsequential ... to affect the integrity of an employee's service and as such is not deemed a conflict." See U.S. Government Accountability Office, *Presidential Transition: Information on Ethics, Funding, and Agency Services*, GAO-17-615R, September 7, 2017, p. 11, https://www.gao.gov/assets/gao-17-615r.pdf#page=11.

[41] H.R. 336, §2. H.R. 336 would require action with 90 days of enactment for current Members, or 90 days of being sworn in for new Members. S. 3494, §2, proposes to add a new section to the Ethics in Government Act, that would require divestiture or placement of covered assets in a qualified blind trust within 30 days of enactment for current Members, or 30 days of being sworn in for new Members.

[42] H.R. 1579, H.R. 6490, H.R. 6694, S. 564, S. 3504, and S. 3612.

[43] National Conference of State Legislators, "Blind Trusts," at https://www.ncsl.org/research/ethics/blind-trusts.aspx.

Each year, the House Ethics Committee and the Senate Select Committee on Ethics review thousands of filings. The addition of qualified blind trusts for hundreds of filers could significantly add to the review and certification burden.[44]

Change to Public Access to Disclosure Filings

Current law requires Members of Congress to file public financial disclosure and periodic transaction reports.[45] For Representatives and Senators, periodic transaction reports and financial disclosure reports are available for public inspection on the Clerk of the House's and Secretary of the Senate's website, respectively.[46] Periodic transaction reports and financial disclosure reports for officers and other covered congressional employees are not available for public inspection.[47]

Four proposals would require additional public access to certain financial disclosure and periodic transaction report related information. H.R. 6694 and S. 3612 would amend the STOCK Act to require public access to covered officials' financial disclosure and periodic transactions reports. H.R. 336 would require the supervising ethics office to post certification for qualified blind trusts on a public website. S. 3494 would require the supervising ethics office to post qualified blind trust certificates, trust agreements, schedules of assets, any extensions granted, and any penalties levied.

Penalties for Non-Compliance

Ten legislative proposals would change available penalties for non-compliance and four legislative proposals do not specify potential changes to penalties. Within the ten legislative proposals, two basic penalty strategies are suggested: fine individuals for non-compliance and/or publish the names of individuals who are found in violation of the law on a public webpage. As noted in **Table 1**, those penalties include

- fines from $500 per case (H.R. 6694 and S. 3612);
- a civil penalty of not less than 10 percent of the value of the covered investment (H.R. 1579, S. 564, H.R. 6694, and S. 3612);
- "disgorgement" to the United States Treasury of any profit from the transaction or holding (H.R. 6490 and S. 3504);

---

[44] Using data from the 116th Congress (2019-2020), the House reported that it received 6,331 financial disclosure reports and 3,722 periodic transaction reports filed by Members, officers, and employees of the House. In the Senate, the Senate Select Committee on Ethics reported that it received 3,712 public financial disclosure and periodic disclosure of financial transactions reports in 2020 and 3,876 public financial disclosure and periodic disclosure of financial transaction reports in 2021. House Ethics Committee, ***Summary of Activities***, 116th Congress, p. 7; U.S. Congress, Senate, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics 117th Congress, First Session," January 29, 2021, at https://www.ethics.senate.gov/public/_cache/files/691e5e65-5b73-4e95-8cdb-de056570cb34/annual-report-for-2020.pdf; and U.S. Congress, Senate, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics 117th Congress, Second Session," January 31, 2022, at https://www.ethics.senate.gov/public/_cache/files/9a2ce840-718c-409b-891f-42f5ebf6f365/annual-report-for-2021.pdf.

[45] 5 U.S.C. Appendix §101; P.L. 112-105, §8, 126 Stat. 295 (2012).

[46] 5 U.S.C. Appendix §105. Forms can be accessed at U.S. Congress, House, Office of the Clerk of the House of Representatives, *Financial Disclosure Reports*, at https://disclosures-clerk.house.gov/PublicDisclosure/FinancialDisclosure; and U.S. Congress, Senate, Secretary of the Senate, "Senate Public Financial Disclosure (Senate Rule 34)," *Public Disclosure*, at https://www.senate.gov/pagelayout/legislative/g_three_sections_with_teasers/lobbyingdisc.htm.

[47] P.L. 113-7, §1(a)(1), 127 Stat. 438 (2013). This law modified the STOCK Act to exempt officers and employees from public, online disclosure of their financial disclosure and periodic transaction reports.

- civil fines of not more than $50,000 if the Attorney General or Special Counsel bring a civil suit before a United States district court and the court determines a fine is warranted (H.R. 6678 and S. 3631);
- a penalty equal to the Member's entire salary for as long as the violation occurs (H.R. 6844); and/or
- a civil penalty equal to the monthly equivalent of the annual rate of pay for the Member, after a written notice from the supervising ethics committee to the Member.

Additionally, H.R. 6844 would require the respective ethics committees to publish the names of individuals found in violation of the proposed amendments.

Under current law, a covered individual who fails to file financial disclosure and/or periodic transaction reports or who files false reports may be subject to certain civil actions, generally after the supervising ethics office investigates the circumstances. Should the supervising ethics office find "reasonable cause to believe [the filer] has willfully failed to file or report or willfully falsified or willfully failed to file information required to be reported," it may refer the case to the Attorney General.[48] Further, the Ethics in Government Act specifies that

> The Attorney General may bring a civil action in any appropriate United States district court against any individual who knowingly and willfully falsifies or who knowingly and willfully fails to file or report any information that such individual is required to report pursuant to section 102. The court in which such action is brought may assess against such individual a civil penalty in any amount, not to exceed $50,000.[49]

Alternatively, the law also provides that the supervising ethics office "may take any appropriate personnel or other action in accordance with applicable law or regulation against any individual failing to file a report or falsifying or failing to report information required to be reported."[50]

For Congress, the House Committee on Ethics and the Senate Select Committee on Ethics provide additional interpretation of penalties for financial disclosure. The House incorporates the financial disclosure requirements into Rule XXVI.[51] The Senate incorporates financial disclosure requirements into Rule XXXIV.[52] Both committees, using identical language, also note that "in addition to Committee action, the EIGA [Ethics in Government Act] authorize[s] the Attorney General of the United States to seek a civil penalty ... again an individual who knowingly and willfully falsifies or fails to file or report any required information."[53]

---

[48] 5 U.S.C. Appendix §104(b).

[49] 5 U.S.C. Appendix §104(a)(1).

[50] 5 U.S.C. Appendix §104(c).

[51] U.S. Congress, House, "Rule XXVI-Financial Disclosure," *Constitution, Jefferson's Manual, and Rules of the House of Representatives of the United States One Hundred Seventeenth Congress*, 116th Cong., 2nd sess., 2021, H.Doc. 116-177 (Washington: GPO, 2021), §1103, p. 1021, at https://www.govinfo.gov/content/pkg/HMAN-117/pdf/HMAN-117.pdf#page=1036.

[52] U.S. Congress, Senate, Committee on Rules and Administration, "Rules of the Senate," at https://www.rules.senate.gov/rules-of-the-senate.

[53] U.S. Congress, House Committee on Standards of Official Conduct, *House Ethics Manual*, "Failure to File or Filing False Disclosure Information," 110th Cong., 2nd sess. (Washington: GPO, 2008), p. 265; and U.S. Congress, Senate Select Committee on Ethics, *Senate Ethics Manual*, committee print, 108th Cong., 1st sess., S.Prt. 108-1 (Washington: GPO, 2003), p. 127.

Amend House Rule XXIII

Two legislative proposals would amend House Rule XXIII, the House Code of Conduct, to add a new section.[54] The new section would state

> A Member, Delegate, or Resident Commissioner may not own the common stock of any individual public corporation.[55]

Amending House Rules to prohibit ownership of individual stocks might require the divestiture of certain assets by Members of the House. As an amendment to the Code of Conduct, jurisdiction over the implementation and enforcement of this proposed rule change would likely be with the House Ethics Committee.[56] A similar proposal to amend Senate Rules has not been introduced.[57]

Amending House Rules rather than amending the Ethics in Government Act or creating a new law could be interpreted as having somewhat more limited affect (e.g., not allowing for restrictions to apply after a Member leaves office and not applying to Senators).[58] Some of the proposals involving changes to law would apply to Members for a period *after* they depart the House.[59]

Concluding Considerations for Congress

In the 117th Congress, CRS identified 14 legislative proposals that seek to limit or prohibit Members of Congress from engaging in certain financial transactions. These measures include a wide-ranging number of proposals. They propose amendments to the Ethics in Government Act and/or STOCK Act, the creation of new law, or amendments to House rules. Taken together, the 14 legislative proposals include a range of options to limit or prohibit certain financial activities. These include prohibiting the holding, purchasing, selling, and active management of covered assets; requiring the use of qualified blind trusts to remediate real or perceived financial conflicts of interest; changing public access for financial disclosure documents; and amending penalties for non-compliance. Each of these options likely has advantages and disadvantages should Congress choose to implement a particular measure as introduced or incorporate various concepts into another measure.

Policymakers may wish to consider the scope of the proposals, the benefits of particular proposals, any potential administrative adjustments that might be necessary to implement a modification of ethics laws, and the potential costs to covered officials to comply with the proposed laws. Subsequently, several questions might be considered. These might include:

---

[54] H.R. 459, §5; and H.Res. 873.

[55] H.R. 459, §5; and H.Res. 873.

[56] House Rule X(g).

[57] Senate rules divide its code of conduct among several rules. These include Senate Rule XXXIV (public financial disclosure), Rule XXXV (gifts), Rule XXXVI (outside earned income), and XXXVII (conflict of interest). For more information, see U.S. Congress, Senate, Committee on Rules and Administration, "Rules of the Senate," at https://www.rules.senate.gov/rules-of-the-senate.

[58] See also, *INS v. Chadha* (45 U.S. 919 (1983)), holding that the actions of one chamber cannot alter the legal rights of those outside the legislative branch. Traditionally, when a Representative or Senator departs the House or Senate, the House Ethics Committee or the Senate Select Committee on Ethics loses jurisdiction over the former Member. For example, House Committee on Ethics notes "As a general matter, the Committee's investigative jurisdiction extends to current House Members, officers and employees. When a Member, officer, or employee, who is the subject of a Committee investigation, resigns, the Committee loses jurisdiction over the individual." House Ethics Committee, *Summary of Activities*, 116th Congress, p. 14; and House Rule XI, clause 3(a)(2).

[59] H.R. 336 and S. 3494.

- Should new requirements apply only to Members of Congress, or also to their spouses and dependent children?
- Should congressional officers and staff be subject to the same disclosure and public access considerations as Members of Congress?
- What penalties are appropriate for violations of new or existing requirements and are proposed penalties sufficient to achieve congressional aims?
- What is the financial cost for establishing qualified blind trusts and how might covered officials pay for the establishment of such trusts?

The CHAIRPERSON. Thank you very much for your testimony and your willingness to continue to work with us as we sort through the various proposals.

Ms. Hempowicz, you are now recognized for five minutes.

STATEMENT OF LIZ HEMPOWICZ

Ms. HEMPOWICZ. Chairperson Lofgren, Ranking Member Davis, and Members of the Committee, thank you for inviting me to testify today about addressing conflicts of interest in Congress as they relate to the owning of individual stocks.

There is no denying that this issue has captured public attention in a unique way. In fact, a strong majority of voters from both major political parties support the congressional stock ban. A FOX News poll recently found seventy percent of those surveyed favored banning Members of Congress and their immediate family and staff from trading stocks.

Those numbers didn't come out of nowhere. An avalanche of eye-opening press coverage has demonstrated a congressional stock-trading problem that ranges from seemingly benign missed public disclosure deadlines to criminal insider trading.

In response, there are now entire online communities dedicated to tracking congressional sales, not only to hold Members accountable, but because many Members of Congress outperform the market and an enterprising few in the public want in on the action.

It is no wonder that the polling reflects an overwhelming desire for change. Congress is listening. More than 125 Members are now co-sponsoring legislation intended to address at least some aspects of this problem. It is encouraging to see elected officials so in tune with what their constituents want.

And so, now, Congress is poised to restrict stock trading by lawmakers with bipartisan support, and we are here to help hammer out the details.

The details are everything. There are several competing bills in both chambers of Congress, and when we see legislation advance, it will either be a first step towards creating real ethics rules for Members of Congress or mere window dressing for legalized corruption.

So, I want to spend the few minutes I have with you today talking about what we at POGO see as some of the important bright lines for you to consider as you move forward.

First, as a floor, we recommend that you require Members of Congress to divest conflicting assets, with the option to put any remaining assets in a blind trust that is subject to new public disclosures.

The logic here is simple: Members of Congress have access to nonpublic information and the power to move markets. We must eliminate opportunities for insider trading and insulate Members from even the perception that they are making decisions based on the benefits to their own financial interest rather than the public interest.

Second, to be meaningful, these requirements must cover spouses and minor children. Again, the reasoning is simple: It is a safe presumption that married partners discuss their work dealings and that a minor child's affairs are under some modicum of their parents' supervision. Now, in both cases, that means the spouse or child also has the same access to market-moving information that the public is so concerned about being misused. In a less generous reading, exempting spouses or minor children would supply an easy, opaque way for a corrupt Member to hide self-dealing and make any added restrictions totally moot.

Third, the new standards cannot exempt assets that were owned before taking office. Unless Members of Congress are willing to recuse from votes or committee assignments based on their financial holdings prior to taking office, an exemption for previously held assets creates a potential conflict without serving any discernible public policy objective.

I want to be clear: POGO wants a much stricter ban than any of those you are considering today. We would limit the holdings that Members, their spouses, dependent children, and senior staffers can own to diversified mutual funds and U.S. Treasury bonds, with narrow exemptions applicable only in truly unusual circumstances.

Today, we have focused our bright lines on improvements to the law that will enhance accountability and public trust related to concerns about insider trading. And there is incredible momentum for these reforms that would respond directly to one of the public's most acutely expressed institutional concerns.

Now, some have suggested that Congress should slow down this current effort so that it may include reforms to the financial-conflicts-of-interest systems that apply to the judiciary and the Executive Branch. You face the very real possibility of passing no reforms if you slow down now. I urge you to focus first on passing restrictions for Congress and then use that momentum to pass additional and, yes, critically necessary conflicts-of-interest reforms to the other branches of government.

I want to close with this thought. The reason we are having this conversation today isn't because of any one scandal or missed STOCK Act filing deadline. We are here because the barrage of the many different examples across both chambers and parties has given the public an overwhelming perception that Congress is engaged in corrupt behavior when Members are allowed to freely own individual stocks.

My colleagues at the Project on Government Oversight stand by, ready to aid in your efforts in addressing this problem however we can.

Thank you again. I look forward to your questions.

[The statement of Ms. Hempowicz follows:]

POGO

PROJECT ON GOVERNMENT OVERSIGHT

Testimony of Liz Hempowicz, Director of Public Policy
Project On Government Oversight
Before the U.S. House of Representatives Committee on House Administration
On "Examining Stock Trading Reforms for Congress"
March 16, 2022

Chairperson Lofgren, Ranking Member Davis, and Members of the Committee, thank you for inviting me to testify on behalf of the Project On Government Oversight (POGO) today, and thank you for holding a hearing on the important issue of congressional stock trading. POGO is a nonpartisan independent watchdog that investigates and exposes waste, corruption, abuse of power, and when the government fails to serve the public or silences those who report wrongdoing. We champion reforms to achieve a more effective, ethical, and accountable federal government that safeguards constitutional principles.

As of this writing, there are 123 Members of Congress cosponsoring legislation to restrict the owning and trading of stocks by Members of Congress.[1] That number continues to increase each week. It is gratifying to see so much bipartisan interest and support for strengthening congressional ethics. Because the American people have spoken out on this, it is not a partisan issue: Members of Congress from across the political spectrum see the need for change.

In fact, a strong majority of voters from both major political parties support a congressional stock trading ban. A Fox News poll recently found 70% of those it surveyed favored "[b]anning current members of Congress and their immediate family and staff from trading stocks."[2]

POGO urges Congress to do the right thing and put the public's interests ahead of its own. We encourage you to ban Members of Congress, their immediate families, and their senior staffs

---

[1] TRUST in Congress Act, H.R. 336, 117th Cong., (2021), https://www.congress.gov/bill/117th-congress/house-bill/336/cosponsors; Ban Conflicted Trading Act, S. 564, 117th Cong., (2021), https://www.congress.gov/bill/117th-congress/senate-bill/564/cosponsors; Ban Conflicted Trading Act, H.R. 1579, 117th Cong., (2021), https://www.congress.gov/bill/117th-congress/house-bill/1579/cosponsors; Ban Congressional Stock Trading Act, S. 3494, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/senate-bill/3494/cosponsors; Bipartisan Ban on Congressional Stock Ownership Act of 2022, H.R. 6678, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/house-bill/6678/cosponsors; Bipartisan Ban on Congressional Stock Ownership Act of 2022, S. 3631, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/senate-bill/3631/cosponsors; Ethics Reform Act, S. 3550, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/senate-bill/3550/cosponsors; STOCK Act 2.0, S. 3612, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/senate-bill/3612/cosponsors; STOCK Act 2.0, H.R. 6694, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/house-bill/6694; Banning Insider Trading in Congress Act, S. 3504, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/senate-bill/3504/cosponsors; Banning Insider Trading in Congress Act, H.R. 6490, 117th Cong., (2022), https://www.congress.gov/bill/117th-congress/house-bill/6490.

[2] Fox News, "Fox News Poll," January 23, 2022, https://static.foxnews.com/foxnews.com/content/uploads/2022/01/Fox_January-16-19-2022_Complete_National_Topline_January-23-Release.pdf.

Project On Government Oversight
1100 13th Street NW, Suite 800
Washington, DC 20005

202.347.1122
info@pogo.org
www.pogo.org

from trading stocks. Specifically, POGO calls for passage of a congressional stock trading ban that merges the best elements of the TRUST in Congress Act (H.R. 336), the Ban Congressional Stock Trading Act (S. 3494), and the Bipartisan Ban on Congressional Stock Ownership Act of 2022 (H.R. 6678; S. 3631).[3] POGO has a recommendation for a much stricter ban that applies more broadly across government, but we emphasize that Congress should act now on the pending bills and take up our stricter recommendation immediately afterward. Congress must not waste the momentum that has gathered behind the current effort to ban congressional stock trading by making the perfect the enemy of the good.

Restricting trades and, ideally, ownership of certain financial interests by Members of Congress, their spouses, and their minor children would — for the first time — create a government ethics program in Congress that puts public duty over private convenience. That is the kind of ethics program America deserves.

A Problem Too Long Ignored

In an opinion on government ethics issues, the Supreme Court cited the ancient maxim that "no man may serve two masters," which it found "especially pertinent if one of the masters happens to be economic self-interest."[4] The court was writing about the executive branch conflict of interest law in that decision, but the maxim holds equally true for Congress.

Unfortunately, some Members of Congress have, thus far, declined to stop serving their economic self-interest. The result has been disastrous for public faith in the institution of Congress.[5] We are here today in large part because Congress has drawn the wrong kind of attention to its Members with trades and conflicts of interest that have, quite understandably, alarmed the public. Even when elected officials have not engaged in criminal insider trading, the appearance of an overlap between their official and personal interests has been enough to undermine the public's trust in the first branch of government.

The public's perception didn't come out of nowhere. A deluge of eye-opening press coverage has demonstrated a congressional stock trading problem that rages from seemingly benign missed public disclosure deadlines to criminal insider trading.[6] In a recent article, *Insider*

---

[3] TRUST in Congress Act, H.R. 336; Ban Congressional Stock Trading Act, S. 3494; Bipartisan Ban on Congressional Stock Ownership Act of 2022, H.R. 6678; Bipartisan Ban on Congressional Stock Ownership Act of 2022, S. 3631 [See note 1].

[4] United States v. Mississippi Valley Generating Co., 364 U.S. 520, 549 (1961), https://supreme.justia.com/cases/federal/us/364/520/.

[5] Megan Brenan, "Americans' Trust in Government Remains Low," Gallup, September 30, 2021, https://news.gallup.com/poll/355124/americans-trust-government-remains-low.aspx.

[6] United States Attorney's Office, Southern District of New York, "Former Congressman Collins Sentenced For Insider Trading Scheme And Lying to Federal Law Enforcement Agents," January 17, 2020, https://www.justice.gov/usao-sdny/pr/former-congressman-christopher-collins-sentenced-insider-trading-scheme-and-lying; Kevin Breuninger, Dan Mangan, and Tucker Higgins, "Ex-New York congressman Chris Collins sentenced to 26 months for insider-trading tip to son," CNBC, January 17 2020, https://www.cnbc.com/2020/01/17/chris-collins-sentenced-to-26-months-for-insider-trading-tip.html. Former Representative Collins was freed after serving less than three months of his sentence only because he received a presidential pardon. See Robert J. McCarthy, "Pardoned by Trump, a contrite Collins returns home a changed man," *The Buffalo News*, December 24, 2020, https://buffalonews.com/news/pardoned-by-trump-a-contrite-collins-returns-

reported on STOCK Act violations by no fewer than 57 Members of Congress.[7] The same publication highlighted the lack of transparency regarding enforcement or compliance with the law, noting that Members and senior staffers have violated the law hundreds of times and only inconsistently incur minor penalties.[8]

I encourage Members of this committee to read this reporting. But instead of summarizing individual examples of real or perceived conflicts of interest, I want to reaffirm that the reason we're having this conversation today isn't because of any one instance. We're here because the barrage of these different examples across both chambers and parties has given the public an overwhelming perception that Congress is engaged is corrupt behavior when Members are allowed to freely trade individual stocks.

There are entire online communities dedicated to tracking congressional stock sales — not to hold Members accountable, but because some members of Congress outperform the market and an enterprising few want in on the action.[9] It's no wonder the polling reflects an overwhelming desire for change.

Despite the public pressure, some Members of Congress have been outright dismissive about the possibility of restricting stock trades. In December, Speaker Pelosi brushed off a question about banning Members of Congress from trading stocks, saying "We are a free-market economy. They should be able to participate in that."[10] House Majority Leader Steny Hoyer (D-MD) echoed the sentiment a month later, suggesting that Members of Congress should be treated the same as members of the public who lack access to nonpublic information and do not wield governmental power. His position is that "members ought not to be in a different situation that

---

home-a-changed-man/article_4a914ae4-4608-11eb-9974-0715d91f7b6b.html (last updated December 25, 2020); Robert Faturechi & Derek Willis, "Senator Dumped Up to $1.7 Million of Stock After Reassuring Public About Coronavirus Preparedness," *ProPublica*, March 19, 2020, https://www.propublica.org/article/senator-dumped-up-to-1-7-million-of-stock-after-reassuring-public-about-coronavirus-preparedness; Katelyn Burns, "Sen. Kelly Loeffler sold at least $18 million more in stocks before the coronavirus crash than previously reported," *Vox*, April 2, 2020, https://www.vox.com/policy-and-politics/2020/4/1/21202900/kelly-loeffler-stock-sales-coronavirus-pandemic; Tobias Hoonhout, "Dem Rep. Sells off Stock Purchase amid Coronavirus Outbreak after Being Confronted," *National Review*, March 25, 2020 https://news.yahoo.com/dem-rep-sells-off-stock-141014443.html; Ryan Nicol, "Brian Mast ends 2021 with second-best stock record in Congress, with help from 'unusual' trade," *Florida Politics*, January 18, 2022, https://floridapolitics.com/archives/487252-brian-mast-ends-2021-with-second-best-stock-record-in-congress-with-help-from-unusual-trade/; "Congressional Trading in 2021," Unusual Whales, January 10, 2022, https://blog.unusualwhales.com/unusual_blog/post/congressional-trading-2021/.

[7] Dave Levinthal, "57 members of Congress have violated a law designed to stop insider trading and prevent conflicts-of-interest, *Insider*, February 15, 2022, https://www.businessinsider.com/congress-stock-act-violations-senate-house-trading-2021-9 (last updated March 3, 2022).

[8] Camila DeChalus, Kimberly Leonard, and Dave Levinthal, "Congress and top Capitol Hill staff have violated the STOCK Act hundreds of times. But the consequences are minimal, inconsistent, and not recorded publicly," *Insider*, December 15, 2021, https://www.businessinsider.com/congress-stock-act-violations-penalties-consequences-2021-12.

[9] Tim Mak, "TikTokers Are Trading Stocks By Copying What Members Of Congress Do," *NPR*, September 21, 2021, https://www.npr.org/2021/09/21/1039313011/tiktokers-are-trading-stocks-by-watching-what-members-of-congress-do; See also "CongressStockWatcher," Reddit, https://www.reddit.com/r/CongressStockWatcher/ and "Congressional Trading in 2021," Unusual Whales [See note 6].

[10] Brian Slodysko, "Pelosi defends lawmaker stock trades, citing 'free market,'" Associated Press, December 15, 2021, https://apnews.com/article/business-nancy-pelosi-congress-8685e82eb6d6e5b42413417f3d5d6775.

they would otherwise be if they weren't members of Congress."[11] Senator Tommy Tuberville (R-AL) colorfully expressed his opposition to a stock trading ban: "I think it's ridiculous. They might as well start sending robots up here." He added, "I think it would really cut back on the amount of people that would want to come up here and serve."[12] Representative Elaine Luria (D-VA) also voiced strong opposition to a stock ban, saying that, despite overwhelming public support for restrictions, "this whole concept is bullshit."[13]

Their outlook is not a new one. In 1962, Congress exempted itself from a new conflict of interest law that applied to executive branch employees, their spouses, their minor children, their general partners, and their prospective employers.[14] But Members of Congress wield far greater power than nearly all of the 2.1 million federal workers who are subject to the federal conflict of interest law. Even so, the lowest entry-level federal employee is subject to stricter ethics restrictions than the powerful Speaker or Minority Leader of the House of Representatives or the Senate's leadership.[15]

Think about that: Elected officials whom the people have entrusted with the power to send Americans to die in wars, tax businesses, respond to crises, and regulate our very lives are subject to far lower standards than entry-level workers in the executive branch. Any service to the nation is noble work but scheduling appointments and making photocopies is far less likely to create conflicts of interest than serving in Congress.

Congress has asked other government officials to make financial sacrifices for public service, but has exempted its Members from this requirement for over half a century.[16] The Senate routinely reviews ethics agreements of presidential nominees to executive branch positions that compel extensive divestitures to ensure compliance with the conflict of interest law.[17] Yet Members of Congress are not subject to that law, despite the fact that they typically serve longer than these presidential appointees.

Former director of the U.S. Office of Government Ethics Walter Shaub and I recently wrote about this topic in an opinion piece for the *Washington Post*. There, we noted that others have tried to water down the notion of a stock trading ban by introducing bills that are too weak to produce meaningful change.[18] Some have introduced bills that fail to cover spouses and minor

---

[11] Mike Lillis, "Joining Pelosi, Hoyer says lawmakers should be free to trade stocks," *The Hill*, January 19, 2022, https://thehill.com/homenews/house/590428-joining-pelosi-hoyer-says-lawmakers-should-be-free-to-trade-stocks.

[12] Eric Garcia, "Repeat STOCK Act violator Sen Tommy Tuberville calls trading ban for Congress 'ridiculous,'" *The Independent*, February 9, 2022, https://finance.yahoo.com/news/repeat-stock-act-violator-sen-193143693.html.

[13] Bryan Metzger, "Rep. Elaine Luria slams proposals to ban stock trading by lawmakers: 'This whole concept is bullshit,'" *Insider*, February 10, 2022, https://www.businessinsider.com/elaine-luria-opposes-stock-trade-ban-lawmakers-2022-2.

[14] 18 U.S.C. § 208 (2021), https://www.law.cornell.edu/uscode/text/18/208.

[15] 18 U.S.C. § 208 [See note 14].

[16] 18 U.S.C. § 208 [See note 14].

[17] Office of Government Ethics, *Guide to Drafting Nominee Ethics Agreements*, at 27, (October 2020), https://www.oge.gov/web/oge.nsf/0/E4716CFB6F236C12852586100004943C7/$FILE/Ethics%20Agreement%20Guide%20October%202020.docx (revised May 26, 2021).

[18] Walter M. Shaub, Jr. and Liz Hempowicz, "Here's how to ban congressional stock trading so politicians can't cheat," *Washington Post*, February 16, 2022, https://www.washingtonpost.com/outlook/2022/02/16/congress-stock-ban-ossoff-warren-hawley/.

children. Relying on these bills would be worse than enacting no ban at all because they would create the illusion of reform without addressing the problem.[19] Others have suggested weak enforcement mechanisms, but we have already seen too little enforcement of the STOCK Act to skimp on enforcement of a congressional stock trading ban.[20] Some proposals would exempt assets Members already own, which would fail to address concerns about conflicts of interest.[21] POGO opposes all of these bills for those reasons. Their sponsors are undoubtedly well-meaning, but their proposed language does not go far enough to solve the problem.

We call on Congress to take a meaningful step forward to reduce conflicts of interest and prevent even the appearance of insider trading. We also urge Congress to be transparent about the process of crafting a congressional stock trading ban. The decision to hold a hearing today is a good start. POGO urges the committee and Congress as a whole to subject any bill and amendments to public debate. Each Member should be clear about where he or she stands on important decisions, including decisions on the question of covering spouses and minor children.

The Solution

As a floor, we recommend that you require Members of Congress and their spouses to divest a broad array of investments with no exception for those held before taking office. Then, require Members to put any remaining assets in a blind trust that is subject to new disclosures about their holdings. The logic here is simple: Members of Congress have access to nonpublic information and the power to move markets. We must eliminate opportunities for insider trading and insulate Members from the perception that they are making decisions based on benefits to their own financial interest and at the expense of the public's interest.

There are numerous pending bills, some of which are strong and some of which are not. I will discuss key concepts, warn about potential pitfalls, and recommend an approach that best responds to the public's concern and capitalizes on this unique momentum.

Key concept: These reforms are straightforward.

Before getting into the complexities of individual proposals, I want to state clearly that a ban on stock trading is not complicated. Yes, exemptions, enforcement, and transparency certainly require some finesse. But opponents of a stock trading ban who try to derail reform by making the issue seem more complicated than it is are ignoring the fact that the executive branch has successfully applied a strict criminal conflict of interest law for over half a century.[22] Some executive branch employees have long been subject to a variety of prohibited stock holding restrictions, which means even mandatory divestiture is not a new issue for the government.[23]

---

[19] See the Ban Conflicted Trading Act, H.R. 1579 and S. 564, [See note 1].
[20] See the Banning Insider Trading in Congress Act, H.R. 6490 and S. 3504, [See note 1].
[21] See the Banning Insider Trading in Congress Act, H.R. 6490 and S. 3504; and the STOCK Act 2.0, H.R. 6694 and S. 3612, [See note 1].
[22] 18 U.S.C. § 208 [See note 14].
[23] See, for example, 10 U.S.C. § 988 (2021), https://www.law.cornell.edu/uscode/text/10/988; 12 U.S.C. § 242-244 (2021), https://www.law.cornell.edu/uscode/text/12/chapter-3/subchapter-II; 15 U.S.C. § 2053(c) (2021), https://www.law.cornell.edu/uscode/text/15/2053; 31 U.S.C. § 329 (2021), https://www.law.cornell.edu/uscode/text/31/329; 43 U.S.C. § 11 (2021),

That it seems novel to Members of Congress owes solely to the fact that Congress chose to exempt its Members from the conflict of interest law for 60 years — and, as we all know, public confidence in the institution has suffered as a result.

In our conversations with congressional offices, my colleagues and I have heard some common questions about the fairness of extending the law to interests in spouses' employers, the ban's applicability to cryptocurrency or real estate, and the misperception that Members will receive statements revealing the holdings of qualified blind trusts — the same questions posed in a recent *Politico* article.[24] But my testimony today addresses these questions and shows the concerns they suggest are not obstacles to Members fulfilling their ethical duty to their constituents.

For example, some of the bills pending before Congress include an exception for interests in a spouse's employer.[25] It will not be difficult to apply the law to spouses whose profession requires them to buy and sell stocks for clients, because the ban would not cover stocks they do not own.[26] When it comes to cryptocurrency and real estate, Congress can follow the lead of the executive branch, which has had no difficulty understanding the application of the conflict of interest law, 18 U.S.C. § 208, to these types of investments.[27] As for blind trusts, there are many misconceptions about how they work and the law that governs them, but they can be clarified, as

---

https://www.law.cornell.edu/uscode/text/43/11; 5 C.F.R. § 3101.108 (2022), https://www.law.cornell.edu/cfr/text/5/3101.108; 5 C.F.R. § 3201.103 (2022), https://www.law.cornell.edu/cfr/text/5/3201.103; 5 C.F.R. § 3401.102 (2022), https://www.law.cornell.edu/cfr/text/5/3401.102; 5 C.F.R. § 4101.102-103 (2022), https://www.law.cornell.edu/cfr/text/5/4101.102, https://www.law.cornell.edu/cfr/text/5/4101.103; 5 C.F.R. § 5501.104 (2022), https://www.law.cornell.edu/cfr/text/5/5501.104; 5 C.F.R. § 5601.102 (2022), https://www.law.cornell.edu/cfr/text/5/5601.102; 5 C.F.R. § 6801.103 (2022), https://www.law.cornell.edu/cfr/text/5/6801.103; 5 C.F.R. §§ 8301.103 and 8301.107 (2022), https://www.law.cornell.edu/cfr/text/5/8301.103, and https://www.law.cornell.edu/cfr/text/5/8301.107; 5 C.F.R. § 9001.104 (2022), https://www.law.cornell.edu/cfr/text/5/9001.104; 5 C.F.R. § 9401.106 (2022), https://www.law.cornell.edu/cfr/text/5/9401.106; 17 C.F.R. § 140.735-2 (2022), https://www.law.cornell.edu/cfr/text/17/140.735-2.

[24] Katy O'Donnell, "Spouses, taxes and crypto: The unanswered questions for Congress' stock trading ban," *Politico*, February 12, 2022, https://www.politico.com/news/2022/02/12/congressional-trading-bans-explained-00008245.

[25] See, for example, the Ban Congressional Stock Trading Act, S. 3494; TRUST in Congress Act, H.R. 336 [See note 1].

[26] See, for example, §2(c) of the Bipartisan Ban on Congressional Stock Ownership Act of 2022, S. 3631, which specifies that "[n]othing in this section shall be construed to prevent … a spouse of a Member of Congress from trading any asset described in subsection (b)(1) that is not owned by the spouse or Member of Congress in the course of performing the primary occupation of the spouse." [See note 1]; Katy O'Donnell, "Spouses, taxes and crypto," [See note 24].

[27] For a discussion of reporting requirements and conflict of interest restrictions, see U.S. Office of Government Ethics, Legal Advisory, "Guidance for Reporting Virtual Currency on Financial Disclosure Reports," LA-18-06, June 18, 2018, https://www.oge.gov/Web/oge.nsf/Legal%20Docs/D9038B8D8DE24D88852585BA005BEC34/$FILE/LA-18-06.pdf?open. See also U.S. Office of Government Ethics, Legal Advisory, "Real Estate Investment Trusts, Master Limited Partnerships, and Business Development Companies: Financial Disclosure Reporting and Conflicts of Interest Considerations," LA-21-02, January 6, 2021, https://www.oge.gov/Web/oge.nsf/Legal%20Docs/84EBAF6D59346CC18525865500670703/$FILE/LA-21-02%20Real%20Estate%20Investment%20Trusts,%20Master%20Limited%20Partnerships,%20and%20Business%20Development%20Companies.pdf?open.

I will explain in the next section. The core concept behind blind trusts is simple: trustees do not let Members know what assets they buy.[28]

Congress has the power to make these policies more complex, but there is no need to do so. Adding an exemption for small business stocks could add complexity, but we don't think Congress should exempt small business stocks from the requirement to place assets in blind trusts. Adding an exemption for stocks a Member held upon taking office could add complexity. But we don't think Congress should exempt those stocks. Adding an exemption for small purchases of stocks could again add complexity. Again, however, we don't think Congress should add a *de minimis* exemption.

One guiding principle will simplify the work of drafting a congressional stock trading ban: Members should resist the temptation to put their personal interests ahead of the public's interest. They should write the law that their constituents would write, erring on the side of prohibiting the sort of conduct that has alarmed the public.

Ultimately, the issue before the committee need not be made complex. A ban on congressional stock trades, after all, is easy to articulate and easy to legislate: Do not trade stocks. Any complexity comes from the creation of tax code-like loopholes and exemptions. POGO stands ready to lend expertise in drafting clear legislative language that addresses any reasonable concerns members may have.

Key Concept: These reforms are reasonable.

All objections predicated on the unreasonableness of a stock trading ban should be dismissed out of hand. No one is calling for Members of Congress to put their money under their mattresses. A consistent position held by almost every commentator on this issue is that Members should be allowed to buy and sell diversified mutual funds. This approach is not novel; it is the one favored by the federal executive branch.[29]

Similarly, any concerns about the reasonableness of covering the holdings of spouses and minor children should also be dismissed. Covering the financial interests of spouses and minor children is necessary to resolve concerns about the appearance of insider trading. The public has no way to know if a Member of Congress discusses nonpublic information at home and should not have to wonder whether that information is influencing trades. Covering the financial interests of the

[28] See, for example, § 102(f)(3)(C)(v) in 5 U.S.C. app. § 102 (2021), https://www.law.cornell.edu/uscode/text/5a/compiledact-95-521/title-I/section-102.

[29] See, for example, 5 C.F.R. § 2640.201 (2022), https://www.law.cornell.edu/cfr/text/5/2640.201. See also sections requiring the purchase of diversified mutual funds or Treasury bonds upon divestiture pursuant to a Certificate of Divestiture, 5 C.F.R. §§ 2634.1003(b), 2634.1006 (2022), https://www.law.cornell.edu/cfr/text/5/2634.1003, https://www.law.cornell.edu/cfr/text/5/2634.1006. While the executive branch has also exempted *de minimis* holdings in publicly traded securities, under 5 C.F.R. § 2640.202, such an exemption would be inappropriate for Members of Congress for two reasons. First, Members of Congress have far more authority than nearly all the 2.1 million executive branch employees. Second, the executive branch's exemption for *de minims* holdings requires aggregation of the value of all holdings affected by a covered governmental matter, and this aggregation requirement would make implementation of the exemption difficult if it were applied more broadly to legislation on which Members of Congress vote.

Member's household would eliminate the appearance of insider trading by eliminating the opportunity for it. We need not debate whether Members are sharing nonpublic information that spouses are misusing; what matters is that the public reasonably perceives a risk of misuse. The very point of an ethics program is to remove risk, not to hope it doesn't materialize. Hope is not an ethics program.

The idea of covering the financial interests of an official's immediate family is not novel: Congress has done exactly that in the executive branch. The primary federal conflict of interest law has applied to the holdings of spouses and minor children of executive branch employees for over half a century. Only now that there is momentum to extend this same principle to Congress is there discussion about the fairness of including immediate family in these regulations. As my colleague, Walter Shaub, and I recently wrote:

> "While working at the Office of Government Ethics, one of us (Shaub) spent over a decade forcing presidential nominees for Senate-confirmed posts to comply with a conflict of interest law that applied to them, their spouses and their minor children. In all those years, no senator picked up the phone after reading a nominee's ethics agreement to complain that making the nominee's spouse divest assets was unfair. Not once."[30]

It is also instructive to remember that Congress currently requires Members to file periodic transaction reports regarding sales and purchases of the assets of their spouses and dependent children under both the Ethics in Government Act and the STOCK Act. This disclosure requirement further underscores the fact that Congress knows the finances of a member's household are inextricably linked.

A bill that does not cover the immediate family of a Member of Congress would be worse than worthless — it would be a distraction, one that creates a false appearance of having solved the problem. POGO will oppose any bill that exempts spouses and minor children of Members from the stock trading ban.

Key Concept: Blind trusts all but eliminate the potential for insider trading.

The qualified blind trust program is a creature of statute, specifically the Ethics in Government Act.[31] Under that law, Members of Congress do not receive statements from trustees revealing the holdings of blind trusts.[32] Instead, they receive quarterly statements indicating only the total value of the trust. The trustees file tax returns for the blind trusts and supply Members with only enough information to complete their personal tax returns without revealing the holdings of their blind trusts.[33] A breach of confidentiality about the holdings of the trust would subject the person

---

[30] Walter M. Shaub, Jr. and Liz Hempowicz, "Here's how to ban congressional stock trading," [See note 18].
[31] 5 U.S.C. app. § 102(f)(3) (2021), [See note 28].
[32] 5 U.S.C. app. § 102(f)(3)(C)(v) (2021), [See note 28].
[33] 5 U.S.C. app. § 102(f)(3)(C)(v) (2021), [See note 28]; Staff of Senate Select Committee on Ethics, 114th Cong., *Qualified Blind Trusts* 17-19 (Committee Print, September 2015), https://www.ethics.senate.gov/public/_cache/files/286a4cf9-5aab-40ef-9a6c-bf2278e79e38/qualified-blind-trusts-guide---october-2020.pdf.

responsible to civil penalties.[34] A Member of Congress does not need to know the holdings of the trust in order to file an annual financial disclosure report, because they are not required to report the holdings of a qualified blind trust.[35]

There are several requirements that make qualified blind trusts useful. All qualified blind trusts must be approved by the relevant ethics committee in advance.[36] As part of the process of setting up the trust, the committee checks to ensure there is no relationship between the Member of Congress and the trustee.[37] As a way of ensuring that the trustee would face professional consequences for any violation, the law requires them to be "a financial institution, an attorney, a certified public accountant, a broker, or an investment advisor" who is independent of the Member of Congress.[38] (The executive branch has gone further by providing that a trustee must be a financial institution, and we recommend Congress do the same.)[39] The trustee must be independent and have full discretion to buy or sell any asset.[40] In setting up the trust, a Member of Congress is allowed to tell the trustee only their general goals, such as "maximizing income or long-term capital gain," but cannot specify the types of holdings desired.[41] Members are not permitted to put assets in the trust unless they are "free of any restriction with respect to its transfer or sale."[42] A Member of Congress can write their trustee to request a distribution of cash or to ask the trustee to divest a conflicting financial interest, but a copy of that communication must be sent to the ethics committee.[43] The law bars other general communications between the Member of Congress and the trustee.[44]

Any bill requiring Members of Congress to place assets in a blind trust must also prioritize transparency. Members of Congress will obviously know what assets they originally add when creating the trust. Under the current system, the trustee of a blind trust also notifies a Member in writing when the trustee has sold off any assets the Member initially placed in the trust. The member and the ethics committee receive this notice, but the public does not.

That information gap leaves Members knowing more about their assets than the public knows.[45] The Ban Congressional Stock Trading Act (S. 3494) addresses this problem by requiring the

---

[34] 5 U.S.C. app. § 102(f)(6) (2021), [See note 28].
[35] 5 U.S.C. app. § 102(f)(2)(A) (2021), [See note 28].
[36] 5 U.S.C. app. § 102(f)(3)(D), (5) (2021), [See note 28].
[37] 5 U.S.C. app. § 102(f)(3)(A)(ii)(II), (III) (2021), [See note 28]; *Qualified Blind Trusts* at 2 and 15, [See note 33].
[38] 5 U.S.C. app. § 102(f)(3)(A)(i) (2021); 5 U.S.C. app. § 102(f)(3)(C)(i) (2021), [See note 28]
[39] 5 C.F.R. § 2634.405(a) (2021), https://www.law.cornell.edu/cfr/text/5/2634.405.
[40] 5 U.S.C. app. § 102(f)(3)(A)(ii)(I) (2021), [See note 28].
[41] 5 U.S.C. app. § 102(f)(3)(C)(vi) (2021), [See note 28].
[42] 5 U.S.C. app. § 102(f)(3)(B) (2021), [See note 28].
[43] 5 U.S.C. app. § 102(f)(3)(C)(vi), (E) (2021), [See note 28].
[44] 5 U.S.C. app. § 102(f)(3)(C)(vii) (2021), [See note 28].
[45] Under the Ethics in Government Act, the trustee is authorized to send a letter advising the Member of Congress that the value of one of these initial assets has fallen below $1,000, as would be the case following sale of the asset, with a copy sent to the relevant ethics committee. The House of Representatives has not published much guidance on qualified blind trusts, but the Senate Select Committee on Ethics has published a sample letter for this purpose. A Senate model qualified trust agreement includes a provision that requires a trustee to send copies of the letter to the trust's grantor, the U.S. Senate Select Committee on Ethics, and the Secretary of the Senate. The problem with this arrangement is that it gives the Member of Congress greater knowledge than the public has with regard to the holdings of the trust. If the Member of Congress has not received this notice of a sale, they know that any asset

relevant ethics committee to post these notices of sale on the committee's website for public viewing.[46] As a result, the bill would put the public on an equal footing with the Member with respect to the Member's holdings. This public awareness of any conflicts of interest would also create at least some pressure on a Member to direct the trustee to divest all assets initially placed in the trust or, better yet, refrain from putting anything other than cash in a blind trust.[47]

Most of the stock trading bills in Congress would require investments to be placed in qualified blind trusts, but a pair of companion bills in the House and Senate would exempt investments Members held when they entered Congress.[48] This exemption serves no public interest, and it undermines the value of these bills. This problem isn't hard to understand: It's why Congress chose not to include any exemption for previously acquired assets in the conflict of interest law applicable to executive branch employees.[49] Including this exemption in the final version of any bill would reveal a desire to continue holding Members of Congress to a lower standard than executive branch employees. For that reason, POGO would oppose any bill that includes an existing-holding loophole.

Pitfall to avoid: Do not delay.

Speaker Pelosi has said that any ban must apply to the other branches of government: "It has to be government-wide."[50] POGO agrees in principle that all branches of government need stronger ethics restrictions, but expanding the pending bills to cover other branches right now is a bad idea.

There is considerable momentum behind the drive to ban Members of Congress and their immediate families from trading stocks, and Congress should not risk losing that momentum by delaying the passage of a congressional stock trading ban while drafting and building support for a broader ban. Though we don't want to invoke the cliché about walking and chewing gum at the same time, recent years have shown that when Congress tries to do everything at once, it often fails to do anything at all. For this reason, POGO strongly encourages Congress to pass the bills that already have momentum, then turn to a set of stricter prohibitions applicable to all three branches. POGO will be submitting a recommendation to support that effort, but we want to avoid any risk of losing this opportunity for the congressional ethics program to take a meaningful step forward.

There is precedent for such an approach. By exempting itself from the conflict of interest law decades ago, Congress has shown that parity among branches has not been a concern for

---

initially placed in the trust remains in the trust. See 5 U.S.C. app. § 102(f)(4)(A) (2021), [See note 28]; *Qualified Blind Trusts* at 6 and 18, [See note 33].
[46] See § 202(f), Ban Congressional Stock Trading Act, S. 3494, [See note 1].
[47] Existing law would allow a Member of Congress to issue such a direction, provided that a copy of the communication is provided to the relevant ethics committee. 5 U.S.C. app. §102(f)(3)(C)(vi)(III), (E) (2021), [See note 28].
[48] See § 4 of the Ban Conflicted Trading Act, H.R. 1579 and S. 564, [See note 1].
[49] 18 U.S.C. § 208(a) (2021), https://www.law.cornell.edu/uscode/text/18/208.
[50] Janet H. Cho, "Pelosi Supports Stock Ban for Congress and Judiciary," *Barron's*, February 9, 2022, https://www.barrons.com/articles/nancy-pelosi-stock-ban-congress-judiciary-51644433862?tesla=y.

Members before now. Therefore, the public would likely question the motivation behind any effort to delay passage of a congressional stock trading ban.

Congress can and should pass a congressional stock trading ban this session, hammering out the final language in the process, and then fast-track a separate bill to impose the same requirements on the judicial branch.

Pitfall to avoid: Do not accept a weak enforcement mechanism.

No matter how broad a ban Congress imposes on its Members, the ban will be ineffective if it has a weak enforcement mechanism. One of the pending bills, the Banning Insider Trading in Congress Act, should be avoided because its enforcement mechanism is virtually guaranteed to fail.[51]

The bill would allow a Member of Congress to demand a vote by the full chamber before the chamber's ethics committee could impose a penalty for any violation. This would not only slow the process, it would also likely cause any enforcement effort to break down into partisan fighting. In the Senate, it would only take 40 Members to preclude a vote or even debate on the penalty. In the House, 218 Members would have to be persuaded to back the imposition of any penalty. Passing a bill with such a weak enforcement mechanism would do little to assuage the public outcry that has led Congress to consider a ban in the first place.

In the extremely unlikely event that the full chamber were to approve a penalty under this cumbersome procedure, the bill arms Congress with little in the way of penalties. The bill theoretically would require disgorgement of "profit" from trades.[52] But, since a purchase does not generate a profit, the penalty only applies to sales. A Member of Congress could continue illegally purchasing assets while in office and avoid penalty by merely waiting until they leave Congress to sell any illegally purchased asset. The bill does authorize a fine, but it fails to specify its amount. In any case, given the potential for profit from such trades, it remains unclear whether an ethics committee could or would impose a fine large enough to deter misconduct.[53]

POGO's Recommendation: Substance of ethics restrictions

POGO would like to see a much more restrictive ban applied to elected officials and top employees of all three branches of government.[54] However, as I've already stressed, we support moving quickly to enact the proposed congressional stock trading ban before taking up broader reform. Specifically, we urge Congress to combine provisions of the TRUST in Congress Act (H.R. 336), the Ban Congressional Stock Trading Act (S. 3494), and the Bipartisan Ban on Congressional Stock Ownership Act of 2022 (introduced in the House as H.R. 6678 and in the Senate as S. 3631). The ban on ownership in H.R. 6678/S. 3631 could apply to the subset of interests currently covered under that bill, and the broader definition of "covered investments" in

[51] Banning Insider Trading in Congress Act, S. 3504 and H.R. 6490, [See note 1].
[52] See § 2 of the Banning Insider Trading in Congress Act, S. 3504 and H.R. 6490, [See note 1].
[53] See § 2 of the Banning Insider Trading in Congress Act, S. 3504 and H.R. 6490, [See note 1].
[54] We are submitting for inclusion in the record a separate document that details POGO's recommendations for when Congress begins the next round of conflict of interest reforms.

H.R. 336 and S. 3494 could apply to assets required to be placed in a qualified blind trust, with the additional disclosure requirements of S. 3494. The enforcement provisions in these bills should also be included in the combined bill.

POGO recommends that Congress merge these bills to strengthen congressional ethics without delay. Two of these bills, S. 3494 and H.R. 336, would require that Members place covered investments in qualified blind trusts as a way of banning trades.[55] The third, H.R. 6678/S. 3631, would ban ownership of several types of investments.[56] These approaches are complementary and could be combined. Congress could adopt the prohibition of ownership as to the narrow set of holdings covered by H.R. 6678/S. 3631 and, at the same time, ban trades involving the broader set of holdings covered by S. 3494 and H.R. 336.

Conclusion

Divesting some assets and placing others in blind trusts, with the option to buy and sell diversified mutual funds, is not too much of a sacrifice for the public to ask our leaders to make. Nobody was ever forced to run for Congress, and every person elected to office asked the public to entrust them with great power. Accepting that power means owing a duty to those who have granted it to you.

The people have a right to demand that Members of Congress always put the public's interests first, avoiding even the appearance of impropriety. But that cannot happen if Members and their families are regularly creating conflicts of interest by buying stocks in individual companies.

Thank you again for giving me the opportunity to testify on behalf of the Project On Government Oversight. We look forward to working with the committee to address this critical issue.

[55] See § 2 of the TRUST in Congress Act, H.R. 336, and § 2 of the Ban Congressional Stock Trading Act (S. 3494), [See note 1].
[56] See § 2 of the Bipartisan Ban on Congressional Stock Ownership Act of 2022, H.R. 6678 and S. 3631, [See note 1].

The CHAIRPERSON. I thank you very much.

Mr. Sherman, you are now recognized for five minutes.

STATEMENT OF DONALD SHERMAN

Mr. SHERMAN. Chairperson Lofgren, Ranking Member Davis, and Members of the Committee, thank you for the opportunity to appear before you today to address the ethics problems created when Members of Congress and their families own or trade individual stocks and other securities.

I am especially grateful for this opportunity to testify before Chairperson Lofgren, who thirteen years ago hired me to join the non partisan staff of the House Ethics Committee.

My organization, Citizens for Responsibility and Ethics in Washington, is a nonpartisan, anti-corruption watchdog committed to ensuring that government officials act ethically on behalf of the people they serve.

It is with this purpose in mind that I encourage Congress to embrace comprehensive legislation that satisfies three principles: one, prohibiting Members from owning and trading stocks and other similar commodities or securities; two, extending this prohibition to Members' spouses and dependent children; and three, incorporating a clear civil penalty that is a significant deterrent and easy to administer.

In addition to these priorities, Congress must also ensure that any relevant oversight and enforcement bodies have the authority and the resources necessary to do their jobs effectively and to provide the public with real transparency.

The ethics problems posed by Members of Congress owning and trading stocks are not theoretical. At the beginning of the pandemic, a moment when public confidence in our government was critical, Congress was rocked by scandal.

Reports of Senators making significant financial transactions following private briefings about the coronavirus pandemic was just the tip of the iceberg. At least 75 Members of Congress owned shares in COVID–19 vaccine makers Pfizer, Moderna, and Johnson & Johnson in 2020. These Members were asked repeatedly to vote on legislation that impacted these companies' share prices.

Similar issues have been spotted in other sectors. For example, fifteen Members that sit on committees overseeing U.S. military policy have financial ties to military contractors worth nearly $1 million.

These facts are both egregious and, sadly, unremarkable.

One reason for this litany of questionable conduct is the weakness of our current legal regime. The STOCK Act, passed in 2012 to ensure that Members do not trade on nonpublic information gained through their government jobs and to enforce public transparency of their holdings, has failed to police this kind of behavior. Exposing STOCK Act violations has proven difficult, in part because periodic transaction reports and financial disclosures are hard to access.

Still, the near-constant drumbeat of repeated and reported violations is a death by a thousand cuts for the credibility of this institution.

Since the passage of the STOCK Act, there have also been significant changes that give individual Members even greater ability to affect the market. Members now have a much larger presence on social media, enabling them to impact corporate stock prices with a single tweet. Congress has expanded the power of committee chairs to issue unilateral subpoenas, and a growing number of Members are conducting oversight from their personal offices. Congressional rules need to change to help address Members' expanded ability to influence the market.

Banning Members from owning or trading individual stocks would address several problems, including: the actual conflicts of interest that arise when they take official actions that impact a company or industry where they or their families have a direct financial stake; the appearance of financial conflicts of interest; and the public outrage over Members appearing to trade on confidential information.

A ban is necessary because, unlike other officials in other branches of government, recusal is not a viable option for Members of Congress. Yet both the Executive and Judicial Branches have higher standards. Merely placing individual assets into a qualified blind trust will not fully address these concerns absent a requirement to sell the original assets.

The ban must also extend to Members' spouses and dependent children to ensure that Members can't simply circumvent the law by transferring their individual assets to a close family member.

Finally, the ban must include an enforcement mechanism that is both clear and significant enough to serve as a deterrent. For example, the legislation should not create a standard of intent that would make enforcement unlikely.

While it is understandable that some Members may have questions about the impact of these reforms on their own or their families' interests, these concerns are not more important than the public's right to know with certainty that the people they choose to write their laws are acting on their behalf and not in the service of their own financial interests.

In closing, the public is right to hold their Representatives in Congress to the highest ethical standards and to demand accountability when those Representatives fail to live up to them. Wide bipartisan majorities are demanding that Congress make changes to address Members' buying and owning stock in industries that they oversee. Banning this practice will help to restore public faith and bolster confidence in our democracy.

Thank you for the opportunity to address the Committee today. I look forward to your questions.

[The statement of Mr. Sherman follows:]

TESTIMONY OF DONALD K. SHERMAN
SENIOR VICE PRESIDENT AND CHIEF COUNSEL
CITIZENS FOR RESPONSIBILITY AND ETHICS IN WASHINGTON (CREW)

HOUSE COMMITTEE ON ADMINISTRATION HEARING ON
"EXAMINING STOCK TRADING REFORMS FOR CONGRESS"

MARCH 16, 2022

Chairperson Lofgren, Ranking Member Davis, and members of the Committee, thank you for the opportunity to appear before you today to address the ethics problems created when members of Congress and their families own or trade individual stocks and other securities.

Background

My organization, Citizens for Responsibility and Ethics in Washington, or CREW, is a nonpartisan anti-corruption and good government watchdog committed to ensuring that our institutions and elected officials act ethically on behalf of the people they serve. It is with this purpose in mind that I encourage you to embrace comprehensive legislation that would ban members of Congress, their spouses, and their dependent children from owning or trading individual stocks, bonds, commodities, futures, or other similar financial instruments. Any reform legislation passed by the Congress should contain bright-line rules that give clear guidance to members and their families and be accompanied by a civil penalty that is a significant deterrent and easy to administer.

In addition to these substantive priorities, Congress must also ensure that any congressional committees or federal agencies with oversight and enforcement responsibilities in this bill have the authority and resources necessary to do their job effectively and provide the American public with appropriate, transparent, and accessible information about compliance.

I applaud the members of Congress, in both parties and both chambers, who have developed numerous pieces of legislation to address this pressing issue. I also applaud the House Administration Committee and its leadership for moving expeditiously to reform stock trading by members.

The task before you now is to draft comprehensive and bold legislation that would address the entirety of the problem at hand. Thankfully, your colleagues have provided you with numerous policy proposals, many of which I encourage you to include in the text of the bill you write. It is critical that Congress rises to this moment; you have a once in a generation chance to address financial conflicts of interest in the legislative branch of our government, and ameliorate the public crisis of confidence in government that they create.

Congressional Stock Trading Undermines Ethics and Policy Making

The threat posed by members of Congress owning and trading individual securities is not theoretical; it undermines the critical work of the entire federal government. At the beginning of the pandemic, a moment when public confidence in our institutions of government was critical, Congress was rocked by a scandal involving concerns about members trading individual stocks as Congress was receiving non-public information about the threat of COVID-19.[1] On March 19, 2020, *ProPublica* broke the news that Sen. Richard Burr (R-NC) had sold between $628,000 and $1.72 million in stock holdings in 33 separate transactions on February 13, 2020, two weeks before the U.S. markets crashed more than 8% on February 28, 2020.[2] Two other Senators, Dianne Feinstein (D-CA) and James Inhofe (R-OK), made trades that also drew scrutiny.[3]

Around the same time, other media[4] outlets[5] revealed that then-Sen. Kelly Loeffler (R-GA) and her spouse had sold up to $3.1 million of individual securities starting on January 24, 2020, the day after she received a confidential briefing on the novel coronavirus.[6] In that period Loeffler and her spouse also purchased between $100,000 and $250,000 worth of shares of the technology company Citrix, which is primarily known for its teleworking software.[7] Then-Sen.

[1] Robert Faturechi and Derek Willis, "Senator Dumped Up to $1.7 Million of Stock After Reassuring Public About Coronavirus Preparedness," *ProPublica*, Mar. 19, 2020, available at https://www.propublica.org/article/senator-dumped-up-to-1-7-million-of-stock-after-reassuring-public-about-coronavirus-preparedness.

[2] Covid-19 Event Timeline: How Covid-19 Virus Events Impacted the S&P 500, Valuation Research Services, https://www.valuationresearch.com/pure-perspectives/covid-19-event-timeline/. The U.S. stock markets began their Covid-19-linked crash on February 20, 2020, a week after Sen. Burr's sell-off. *See* https://finance.yahoo.com/quote/%5EDJI/history?period1=1577836800&period2=1585353600&interval=1d&filter=history&frequency=1d&includeAdjustedClose=true.

[3] Eric Lipton and Nicholas Fandos, "Senator Burr Sold a Fortune in Stocks as GOP Played Down Coronavirus Threat," *New York Times*, Mar. 19, 2020, https://www.nytimes.com/2020/03/19/us/politics/richard-burr-stocks-sold-coronavirus.html.

[4] Christina Wilkie, "Two GOP senators face questions over stock sales ahead of the market's coronavirus slide," *CNBC*, Mar. 20, 2020, https://www.cnbc.com/2020/03/20/senators-face-questions-over-stock-sales-before-the-coronavirus-slide.html

[5] Lachlan Markay, William Bredderman, and Sam Brodey, "Sen. Kelly Loeffler Dumped Millions in Stock After Coronavirus Briefing," *The Daily Beast*, Mar. 20, 2020, https://www.thedailybeast.com/sen-kelly-loeffler-dumped-millions-in-stock-after-coronavirus-briefing.

[6] United States Committee on Health, Education, Labor, and Pensions, "Senate Health Committee Announces Briefing to Update Senators on Coronavirus," Press Release of Jan. 23, 2020, https://www.help.senate.gov/chair/newsroom/press/senate-health-committee-announces-briefing-to-update-senators-on-coronavirus.

[7] Markay, Bredderman, and Brodey.

David Perdue (R-GA) also purchased shares in companies that stood to benefit from the pandemic, including, for example, up to $260,000 worth of shares of Pfizer between February 26 and 28, 2020, the middle of the market downturn.[8] Both Senators were dogged by allegations of ethical misconduct and lost their bids for re-election less than a year later.

While these Senators' transactions were deeply problematic, as CREW explained in a letter to the Senate Select Committee on Ethics,[9] their impact was far greater than their legal and political fallout: they conveyed to the public the impression that their representatives were profiting off their positions. And in doing so, they diminished the public's trust in their government and undermined the institutions tasked with responding to an unprecedented crisis of public health at the worst possible time.[10]

The Current Legal Regime is Inadequate to Track or Deter Misconduct

There could not be a better example of the real-world consequences of members of Congress trading or owning individual stocks, bonds, or other similar financial instruments. But it is by no means the only, or even the most problematic instance. *Business Insider* revealed, for example, that in 2020, at least 75 members of Congress owned shares in companies such as Pfizer, Moderna and Johnson & Johnson, that made COVID-19 vaccines, treatments, and tests.[11] These members were asked, repeatedly, to vote on legislation that had a direct impact on these companies' share price. Perhaps even more troubling, recent reporting indicates that at least 15 members of Congress who sat on House and Senate committees that oversee US military policy, had "financial ties to prominent defense contractors that together were worth nearly $1 million in

---

[8] Stephanie Saul, Kate Kelly and Michael LaForgia, "2,596 Trades in One Term: Inside Senator Perdue's Stock Portfolio," *New York Times*, Dec. 2, 2020, https://www.nytimes.com/2020/12/02/us/politics/david-perdue-stock-trades.html.

[9] Citizens for Responsibility and Ethics in Washington, *Letter to the Senate Select Committee on Ethics Requesting an Investigation of Sens. Richard Burr and Kelly Loeffler*, Mar. 20, 2020, https://www.citizensforethics.org/wp-content/uploads/legacy/2020/03/2020-3-20-Burr-and-Loeffler-insider-trading.pdf. The Department of Justice has since closed its investigation into potential insider trading. *See* Ryan Lucas, "Justice Department Closes Investigations of 3 Senators; Burr Inquiry Continues," *National Public Radio*, May 26, 2020, https://www.npr.org/2020/05/26/862692569/justice-department-closes-investigations-of-3-senators-burr-inquiry-continues, and Vanessa Romo, "DOJ Drops Insider Trading Investigation of Sen. Richard Burr," *National Public Radio*, Jan 19, 2021, https://www.npr.org/2021/01/19/958622574/doj-drops-insider-trading-investigation-into-sen-richard-burr.

[10] Kedric Payne, Delaney Marsco, and Sophia Gonsalves-Brown, "Congressional Stock Trading During Pandemic Diminishes Public Trust," *Campaign Legal Center*, Apr. 28, 2020, https://campaignlegal.org/update/congressional-stock-trading-during-pandemic-diminishes-public-trust.

[11] Camila DeChalus , Kimberly Leonard, Warren Rojas, and Madison Hall, "As the pandemic raged, at least 75 lawmakers bought and sold stock in companies that make COVID-19 vaccines, treatments, and tests," *Business Insider*, Dec. 13, 2021, https://www.businessinsider.com/lawmakers-bought-sold-covid-19-related-stocks-during-pandemic-2021-12.

2020."[12] While some of the members reported divesting from owning individual stocks, these facts are both egregious and, sadly, unremarkable.

These very public instances where members' individual stock holdings created conflicts of interest demonstrate the weakness of the current legal regime. The STOCK Act, passed in 2012 to bar members from trading on non-public information gained through their government jobs, give the public some insight into member finances--and to punish members who failed to disclose their holdings and transactions--has failed to deter unethical behavior. It has repeatedly proven unwieldy and hard to enforce. A recent *Business Insider* report revealed that 57 members of Congress recently violated the Act.[13] Exposing these violations was only possible because of rigorous research conducted by media outlets and good government groups, because the access to periodic transaction reports, financial disclosures, and other documents is onerous and expensive for members of the general public. Congress's credibility suffers a death by a thousand cuts thanks to the constant reports of STOCK Act violations. Reform is necessary to address a deficient compliance, transparency, and enforcement regime.

In the decade since the STOCK Act was enacted, there have also been significant changes in the way Congress operates that give individual members even greater ability to impact the market. Members of Congress now have a much larger presence on social media, powerful platforms that can reach millions of Americans. A member can impact corporate stock prices with a single post or tweet. A 2020 Pew Research Center study found that while "a small group of lawmakers with extremely large followings dominate the congressional social media narrative … Congress as a whole produces a vast amount of social media content each month."[14]

Since 2012, Congress has also expanded the power of committee chairs to issue unilateral subpoena authority to compel testimony and information, which has been the source of significant attention from the legal community in advising corporate clients.[15] In recent years, many members have also conducted oversight as Ranking Members[16] or from their individual

[12] Warren Rojas, Camila DeChalus, Kimberly Leonard, and Dave Levinthal, "At least 15 lawmakers who shape US defense policy have investments in military contractors," *Business Insider*, Dec. 13, 2021, https://www.businessinsider.com/congress-members-are-trading-defense-stocks-while-shaping-military-policy-2021-12.

[13] Dave Levinthal, "57 members of Congress have violated a law designed to stop insider trading and prevent conflicts-of-interest," *Business Insider*, Feb. 15, 2022, https://www.businessinsider.com/congress-stock-act-violations-senate-house-trading-2021-9.

[14] Patrick Van Kessel, Regina Widjaya, Sono Shah, Aaron Smith, and Adam Hughes, "Congress Soars to New Heights on Social Media," *Pew Research*, Jul. 16, 2020, https://www.pewresearch.org/internet/2020/07/16/congress-soars-to-new-heights-on-social-media/.

[15] Jamie Gorelick and Benjamin A. Powell, "Expanded Subpoena Powers in New Congress," *WilmerHale Client Alert*, Jan. 20, 2015, https://www.wilmerhale.com/en/insights/client-alerts/expanded-subpoena-powers-in-new-congress.

[16] *See, e.g.*, United States Senate Committee on Homeland Security and Government Affairs, "Rising Emergency Room Costs in Missouri is Focus of McCaskill Inquiry," Press Release of Sep. 25, 2017,

offices,[17] and have added oversight staff to their personal office staff.[18] While these practices bolster Congress's ability to conduct accountability and oversight, they also expand each members' ability to influence the market.

Congress must adjust its rules to keep up with these developments.Without Congressional action, the routine crises of public confidence that result from STOCK Act violations and allegations that members of Congress are overseeing industries where they have a direct financial interest based on their stock portfolio will continue to happen. And the toll they take on our government will only increase.

Let me be perfectly clear: while it is understandable that some members may have concerns about the impact of these reforms on their own portfolios or their families' interests, they also need to remember that public service is a public trust. While some members may be worried about the nuisance of these measures, or the impact they may have on their dependent children's trust structures, these concerns do not trump the public's right to know, with certainty, that the people they choose to write their laws are acting on their behalf--and not in service of their own financial interests.

CREW's Priorities for Legislative Reform

Every person in whom the people repose power, from the power to make law or declare war to the power to write a local ordinance, is bound by that basic ethical principle. Congress has an opportunity to lead and implement ethical reforms that can trickle down to state and local legislative bodies as well. With that in mind, I encourage you to develop legislation that is clear and comprehensive. By "clear," I mean that any reasonable person could understand what the legislation requires, and the means by which those requirements can be met. And by "comprehensive," I mean that the legislation must include a complete ban on members, their spouses, and their dependent children owning or trading individual stocks, bonds, commodities or other similar financial instruments.

The legislation you develop should satisfy three principles:

---

https://www.hsgac.senate.gov/media/minority-media/rising-emergency-room-costs-in-missouri-is-focus-of-mccaskill-inquiry.

[17] *See*, *e.g.*, Authority of Individual Members of Congress to Conduct Oversight of the Executive Branch, 41 Opp. Office of Legal Counsel, May 1, 2017, https://www.justice.gov/olc/file/966326/download#:~:text=The%20constitutional%20authority%20to%20conduct,subcommittees%20(or%20their%20chairmen).

[18] *See*, *e.g.*, Yuki Noguchi, "'No Meaningful Oversight': ICE Contractor Overlooked Problems at Detention Center," *National Public Radio*, Jul. 17, 2019, https://www.npr.org/2019/07/17/741181529/no-meaningful-oversight-ice-contractor-overlooked-problems-at-detention-centers.

1. It should prohibit members from trading and owning individual stocks and other similar securities;
2. The prohibition should extend to members' spouses and dependent children; and
3. It should incorporate a clear civil penalty that is easy to enforce.

Below, I discuss each of these principles and direct the Committee to the specific components of existing legislation that would best advance each principle. I encourage the Committee to craft a new bill that draws from the best individual elements of existing legislation.

Prohibit the trading or ownership of stocks and other similar securities

The legislation must include a comprehensive ban on trading or owning individual stocks and other similar securities. This prohibition is crucial because it would address three key problems: (1) the actual conflicts of interest that arise when members of Congress take official actions that impact a company or industry where they or their families have a direct financial stake; (2) the public outrage over members appearing to trade on confidential information; and (3) the appearance of financial conflicts of interest. The only way to address all three issues is by banning members and their families from trading and owning individual securities.

Anything short of a ban will not fully address the problems you have been charged with solving. Members who have a keen sense of their portfolio, or who are allowed to trade some sub-category of stocks, will still have actual and potential conflicts of interest. A ban is necessary because unlike congressional staff, or officials in other branches of government, recusal is not a viable option for Members of Congress elected to represent their constituents in the legislative branch. Only a complete prohibition will circumvent both real and perceived conflicts, and the damaging second-guessing of members that occurs when those conflicts inevitably become public. This isn't about forcing members of Congress to take a vow of poverty. There are many ways to invest money that don't come with the risk of creating conflicts, including diversified mutual or index funds. This is not a new or outlandish concept: 40% of the members of the 117th Congress already make exclusive use of these investment vehicles.[19]

Placing individual assets into a qualified blind trust ("QBT"), absent a requirement to sell the original assets, is not a sufficient solution to the conflicts that these assets present. In general, QBTs are a vehicle which a potentially conflicted individual could use to divest their assets without dumping their holdings at a potentially inopportune time. The individual places their assets into a QBT and the trustee in their discretion may sell the assets over a period of time to reasonably ensure that they get a fair return on their investments. The trustee is free to invest the proceeds from the sale as they see fit. At that point the trust assets would become "blind."

[19] Campaign Legal Center, *Congressional Stock Trading By the Numbers - 117th Congress*, Feb. 18, 2022, https://campaignlegal.org/document/congressional-stock-trading-numbers-117th-congress.

But a trust is only "blind" when the beneficiary does not know what assets the trust holds, and for the QBT structure to fix the problem presented by stock ownership, it must be fully blind. This means that trustees must be directed to sell all the member's individual stocks, and members must not be permitted to retain any individual stocks held prior to joining Congress.

While I applaud the bi-partisan and bicameral groups of representatives and senators who have introduced legislation that seeks to address this problem, one in particular stands out in this respect: Rep. Jayapal and Rep. Rosendale's Bipartisan Ban on Congressional Stock Trading Act, H.R. 6678 ("BBCSTA" or "Jayapal-Rosendale").[20] Specifically, the BBCSTA bans members of Congress from owning individual stocks, bonds, or other similar financial instruments, and requires that all members divest of all such assets within 180 days. The language is clear and the policy is comprehensive.

Extend the prohibition to members' spouses and dependent children

The ban outlined in our first recommendation must extend to members' spouses and dependent children, such that there is a comprehensive prohibition on members' spouses or dependent children owning or trading individual financial assets.

The importance of extending the ban to cover members' spouses and dependent children is self-evident: members must not be permitted to simply transfer their individual assets to a close family member to circumvent the law. A carve-out for spouses and dependent children would undermine much of the purpose of the legislation and allow the conflicts of interest that result from the ownership of individual assets to remain. This same principle holds in relation to the problem of public confidence: a spouse or dependent child who appears to profit from a member's actions or knowledge of the market is just as damaging to the public's perception of our government as a member profiting themselves. This restriction is also restrained, excluding other close familial relationships including members' parents and adult children, who have also drawn public attention and ethics concern because of their financial dealings.

The legislation that best covers this policy is Sen. Ossoff and Sen. Kelly's Ban Congressional Stock Trading Act, S. 3494 ("BCSTA" or "Ossoff-Kelly"), and its companion, Rep. Spanberger and Rep. Roy's TRUST in Congress Act, H.R. 336.[21] This legislation's text is clear, and the policy is unambiguous: spouses and dependent children are held to the same standard as the members themselves.

[20] Specifically, subsection (b).
[21] Specifically, Section 202(a)(2)(A)).

I understand that some also call for including senior Congressional staff in any legislation that would ban members and their close relatives from owning or trading individual financial instruments. Senior staff play a critical role in our government, and therefore exert an outsize influence on the policymaking process. There are real and serious questions about the propriety of senior Congressional staff owning or trading individual stocks, especially given the recent revelations that 182 senior staff members violated the STOCK Act.[22] But these issues are materially different and substantially less concerning than those presented by members and their close relatives owning or trading individual financial instruments.

First, there is the simple, yet important, fact that members are the people whom the public has elected and entrusted with the authority to make law. While senior staff members can and often do wield a lot of influence over a member's thinking, they are not the people who vote on legislation. Members must be held to the highest standards of ethical conduct because they are the people's representatives in Washington. Staff are ultimately responsible to their employing members and can be fired or disciplined for engaging in behavior that the member believes is unethical or inconsistent with their values. Members are accountable to the public and the ethics rules should reflect these distinctions. Second, there is the practical fact that senior Congressional staff have the ability to recuse themselves to avoid working on issues that might create a conflict of interest. Members of Congress cannot recuse themselves from voting on legislation without depriving their constituents of their constitutional right to be represented in our government.

All of this counsels against including senior Congressional staff in this legislation. Theirs is a separate issue and may require a different approach.

Incorporate a clear civil penalty that is easy to enforce

The legislation must include an enforcement mechanism that is both clear enough that members understand precisely what will happen should they violate the law, and significant enough to serve as a comprehensive deterrent. These two elements are worth discussing separately.

First, it is crucial that Members understand that they will be subject to punishment or civil penalties if they violate the act. The critical element here is the certainty that there will be accountability if they violate the law: decades of academic research demonstrate the centrality of this element to any enforcement regime.[23] This is a key problem with many of the current rules

[22] Kimberly Leonard, Warren Rojas, and Camila DeChalus, "At least 182 high ranking congressional staffers have violated a federal conflicts-of-interest law with overdue disclosure of their personal stock trades," *Business Insider*, Dec. 13, 2021,
https://www.businessinsider.com/congress-staff-violated-stock-act-conflicts-of-interest-possible-2021-12.
[23] *See, e.g.*, Valerie Wright, "Deterrence in Criminal Justice: Evaluating Certainty vs. Severity of Punishment," The Sentencing Project, Nov. 2010,
https://www.sentencingproject.org/wp-content/uploads/2016/01/Deterrence-in-Criminal-Justice.pdf.

regulating Congressional ethics: not only are the rules themselves convoluted and hard to understand, the ethics committees are often permissive in their guidance on and enforcement of violations even when they find them. This is precisely why this element is so important: members are used to a permissive Congressional ethics regime; if they believe that the ban on stock ownership is similarly dysfunctional and unenforceable, some will not take compliance seriously.

For these reasons, the legislation should not create a standard of intent that would make enforcement unworkable or unlikely. A clear and comprehensive ban on owning or trading individual financial instruments should not require that the enforcing authority prove intent at all: either the member owns an individual stock, bond, commodity, or other similar financial instrument within the prescribed period or they don't. It simply doesn't matter what the member intended. Adding an intent requirement to this legislation would only serve to make enforcement less likely; and a stringent standard, such as requiring proof that a member "knowingly" violated the act, could make the entire legislation unenforceable.

Second, the penalty for violating the ban must be substantial enough that members are actually deterred. This self-evident policy is critical in the context of regulating the ownership or trading of individual financial instruments: each transaction, each individual stock, will come with a value calculation, and if the penalty for violating the ban is negligible, then the calculation may favor violating the ban. This is the general theory of deterrence, and while it is worth evaluating its effectiveness in certain criminal justice scenarios, its value in financial circumstances is clear.

I am happy to say that this is an area of policy strength for many of the outstanding pieces of legislation. However, I would encourage the Committee to consider a hybrid approach: include each type of civil penalty, whichever is greatest. Specifically, I would recommend the civil penalties in Ossoff-Kelly and Jayapal-Rosendale, and the disgorgement of gains provision in Rep. Hartzler's Banning Insider Trading in Congress Act, H.R. 6490, whichever is greater.

Conclusion

The Committee on House Administration is tasked with developing legislation to respond to the growing crisis in public confidence arising from members owning or trading individual stocks, bonds, and other similar financial instruments. The public's justifiable and predictable outrage over the various instances at the beginning of the pandemic where members appeared to trade on confidential information has not subsided. Instead, it has fed the growing distrust in Congress as an institution.

The public is right to hold their representatives to the highest of ethical standards, and to demand accountability when those representatives fail to live up to them. Wide bipartisan majorities believe that the Congress should hold itself accountable for these abuses by passing legislation that would impose limits on members and their families from owning and trading certain financial instruments. Designing and passing clear and comprehensive legislation that bans members of Congress, their spouses, and their dependent children, from owning or trading these financial instruments will help to address this crisis of confidence in government. And you will halt the deluge of stories documenting members' questionable stock sales that will continue to undermine confidence in Congress's commitments to ethics and democratic governance.

Thank you for the opportunity to address the Committee today. I look forward to answering your questions and working with the Committee as you design this critical legislation.

The CHAIRPERSON. Thank you.

We will turn now to Professor Nagy for five minutes.

STATEMENT OF DONNA NAGY

Ms. NAGY. Chairperson Lofgren, Ranking Member Davis, and Members of the Committee, thank you for inviting me to testify.

I have been teaching and writing about corporate and securities law for more than 27 years. For nearly half of that time, I have also been writing about government ethics.

What first drew me to that field were the controversies that resulted in the STOCK Act of 2012. I had the great privilege of testifying about insider-trading law in the House and Senate hearings that preceded that legislation.

In connection with today's hearing, what I can also bring to this table are my years of studying how conflicts of interest undermine the legitimacy of decisionmaking by officials entrusted with power.

Whether the decisionmaking occurs by corporate directors inside a boardroom or by lawmakers here in the Capitol, financial conflicts of interest contribute to a corrosive belief that those entrusted with power are making self-serving decisions that may not be in the best interest of those they have been elected to serve.

My testimony today strongly supports your efforts toward reform, and I have four points to highlight.

The first emphasizes a key difference in the many bills I have reviewed. Whereas some seek to restrict the ownership of certain investments by Members of Congress, others seek to restrict only the trading of such investments during congressional service.

In my view, trading restrictions alone will not be an effective solution to the conflict-of-interest problem that is plaguing Congress. Successful reform must also reduce lawmakers' opportunities for personal gains in their investment portfolios when they sponsor, support, oppose, and vote on legislation.

So, I urge this Committee to focus on ownership and not merely trading. What is most needed, in my opinion, is a Federal statute that prohibits Members of Congress and their spouses and dependent children from owning the securities of individual, publicly traded companies.

My second point contrasts the lax conflict-of-interest restraints that currently operate in the Legislative Branch with the very strict anti-conflict laws that Congress has enacted for officials in the Executive and Judicial Branches.

To be sure, ethic rules in both chambers prohibit Members from deriving personal financial benefit from congressional service. But longstanding interpretations permit and facilitate a lawmaker's ability to work and vote on legislation likely to affect their own investments so long as they are not the sole beneficiaries.

The lack of parity among the three branches underscores the urgent need for reform.

My third point refutes the notion that public disclosure of personal investments coupled with the discipline of the electoral process can adequately deter these troubling financial conflicts.

Neither annual ownership disclosures nor specific 45-day transaction reporting has managed to deter lawmakers from owning and trading hundreds of millions of dollars in stock in companies subject to their oversight. If anything, it has made the perception of corruption worse, because, thanks to journalists and good-government groups, the American public now sees even more quickly how frequently and extensively some lawmakers are benefiting from their legislative activity.

Moreover, self-interested legislative activity affects the entire country, whereas only voters in a Member's district or State can have a say in whether conflicts are serious enough to warrant an electoral defeat.

My final point relates to insider trading. Notwithstanding the clarity brought about by the STOCK Act, investigating suspicious trading by congressional officials has proven to be more challenging for the SEC and the DOJ than most may have supposed a decade ago. The Constitution's Speech or Debate Clause puts in place a very high hurdle for obtaining evidence that relates to what a congressional official learned through legislative activity, and, without evidence, prosecutions are not possible.

This hearing constitutes a monumental step toward bringing about real and profound change. I am truly honored to be a part of it. I look forward to your questions, and I stand ready to be of whatever help I can as the legislative process progresses.

Thank you very much.

[The statement of Ms. Nagy follows:]

Examining Stock Trading Reforms for Congress
Hearing Before
the U.S. House of Representatives Committee on House Administration

Testimony of Donna M. Nagy, C. Ben Dutton Professor of Business Law
Indiana University Maurer School of Law
Bloomington, Indiana

April 7, 2022

Chairman Lofgren, Ranking Member Davis, and Members of the Committee: Thank you for inviting me to testify as part of your hearing on "Examining Stock Trading Reforms for Congress." My name is Donna Nagy, and I am the C. Ben Dutton Professor of Business Law at Indiana University Maurer School of Law in Bloomington, Indiana. I have been teaching and writing about corporate law and federal securities law for more than 27 years. For nearly half of that time, I have also been researching and publishing about government ethics. What first drew me to that field were the congressional insider trading controversies that resulted in the passage of the STOCK Act of 2012. In the hearings that preceded that legislation, I had the great privilege of testifying about federal insider trading law before the House Financial Services Committee and the Senate Committee on Homeland Security and Governmental Affairs.

In connection with today's hearing, what I also can bring to the table are my years of studying how conflicts of interest can undermine the legitimacy of decision-making by officials entrusted with power, as well as how the law can operate to guard against such conflicts. Indeed, whether the decision-making occurs by corporate directors inside a boardroom or by lawmakers here in the Capitol, financial conflicts of interests contribute to a corrosive belief that those entrusted with power are making decisions that may serve their own personal gain rather than the best interests of the persons they were elected to serve. I have emphasized this point in much of my scholarship, but particularly so in an article I published nearly a decade ago entitled "*Owning Stock While Making Law: An Agency Problem and a Fiduciary Solution*."[1]

This Committee has a weighty task before it. Over the last several months, at least a dozen bills relating to securities trading reforms have been introduced in the House and the Senate. As I understand it, this Committee was asked to review these proposals and develop consensus legislation that responds to the escalating crisis in confidence that has

[1] Donna M. Nagy, *Owning Stock While Making Law: An Agency Problem and a Fiduciary Solution*, 48 WAKE FOREST LAW REVIEW 567 (2013). My other articles in the area of government ethics include: *Insider Trading, Congressional Officials, and Duties of Entrustment*, 91 BOSTON UNIV. L. REV. 1105 (2011) and *Selective Disclosure by Federal Officials and the Case for an FGD (Fairer Government Disclosure) Regime*, 2012 WISCONSIN L. REV. 1285 (2012) (co-authored with Richard W. Painter). Professor Painter and I built from those articles, as well as his highly regarded work, in a December 2020 letter we co-authored to Senior Leadership of Congress, and some of my testimony draws from that letter.

arisen from lawmakers owning and trading stocks and other financial interests in companies and industries that are directly and substantially affected by legislative activity.

My testimony today strongly supports your efforts toward legislative reform, and it divides into four parts. The first part highlights what I see as the principal difference among the bills and shares my view as to the type of reform that is likely to be most effective. Part two contrasts the strict anti-conflict laws that Congress has enacted for federal officials in the executive and judicial branches with the lax conflict-of-interest restraints that operate in the legislative branch. The third part refutes the rationales put forth in the past by Congress to justify the view that lawmakers' financial conflicts are best deterred through public disclosure of personal investments and the discipline of the electoral process. And the final part discusses why, notwithstanding the clarity brought about by the STOCK Act, troubling insider-trading problems will continue to arise unless and until there is additional legislative reform.

I. Effective Reform Requires an Outright Prohibition on the Ownership of Securities in Publicly Traded Companies

There is one key difference in the many bills I have reviewed in preparation for this hearing: whereas some of the bills seek to restrict the *ownership* of certain securities and other financial investments by Members of Congress, other bills seek to restrict only the *trading* of certain investments while a member is serving in Congress. In my view, trading restrictions alone will not be an effective solution to the conflict-of-interest problem that is plaguing Congress and fostering the public perception of widespread corruption. What is needed is legislation that reduces the widespread belief that—whether accurate or not—many lawmakers are seeking to generate gains and avoid losses in their portfolios when they sponsor, support or oppose, and ultimately vote on legislation. I urge this Committee to focus on the problem of the ownership of certain investments, and not merely the trading of such instruments.

What is most needed, in my opinion, is a federal statute that prohibits Members of Congress and their spouses and dependent children from owning the securities of individual publicly traded companies as well as certain other financial investments that likely will conflict with their official duties. Senior staff of Members of the House and Senate, as well as senior staff of House and Senate committees, should likewise be required to divest, although more flexibility could be given to staff members who choose to recuse from a particular matter as an alternative to divestment. Members of Congress should be available to vote on matters before Congress, but staff members can more easily recuse if divestment is burdensome for them or for a spouse.

Because the reform I favor would mandate outright divestment of individual stocks and certain other investments, I would also suggest coupling that requirement with a provision enabling congressional officials and spouses/dependent children to convert the proceeds from their sales of individual stocks and other proscribed investments into either diversified investment funds that are widely held or Treasury securities while deferring any capital gains taxes until they sell those new investments. Congress has previously amended the tax code to allow for the deferral of capital gains when an executive branch official converts assets into permissible investments to avoid conflicts of interest,[2] and fairness should dictate that a similar provision apply to the legislative branch.

As an alternative to requiring outright divestment of individual stocks and certain other financial investments, multiple bills under consideration would instead permit Members of Congress to hold such assets in a "qualified blind trust" (QBT). Although the use by Members of QBTs would adequately address the serious concerns about congressional insider trading, the placement of accumulated assets into QBTs is only a minimally effective anti-conflict measure because the trust will not actually be blind to the Member unless and until the trustee sells off all the original assets and purchases new ones in their place. As such, QBTs will not do much to reduce the public perception that lawmakers sponsor and vote for bills to increase the value of their investments. QBTs are also complicated to organize and expensive to maintain, which may explain why fewer than a dozen Senators and Representatives currently utilize QBTs. In addition, there is little reason to be optimistic about Congress's ability to adequately monitor compliance with the terms of so many additional QBTs. Press reports indicate that the STOCK Act's 45-day reporting requirement for securities transactions is routinely disregarded by congressional officials with little consequence. Accordingly, the logistical challenges that would be presented by widespread use of QBTs in Congress seem immense.

Moreover, whether or not held in a QBT, there is no compelling financial reason to own individual stocks today, and only a small fraction of the U.S. public (about 15%) does so. Modern portfolio theory holds that most stocks are efficiently priced based on publicly available information—there being no obvious "bargains" to be had in publicly traded markets. To the extent there are such bargains to be found, it is also likely that many professional portfolio managers at mutual funds are much better stock pickers than some of the trustees of the QBTs who would be looking to be compensated generously for their services in selling the lawmakers' original assets and in purchasing and trading the assets that would be kept blind. And it is almost certainly the case that professional portfolio managers at mutual funds are much better stock pickers than individual Members of Congress who are both complying with federal insider trading law and not using their legislative activity to affect the value of the companies in which they hold investments.

[2] See RICHARD W. PAINTER, GETTING THE GOVERNMENT AMERICA DESERVES: HOW ETHICS REFORM CAN MAKE A DIFFERENCE (Oxford U. Press 2009) at 42 (discussing 5 CFR 2634.1006's provision for a rollover into permitted property).

II. Stringent Anti-Conflict Laws Apply to Executive and Judicial Branch Officials, Whereas Congress Has Not Only Tolerated But Also Facilitated its Own Members' Financial Conflicts

Federal officials—whether elected or appointed—are entrusted with political power, and they are thus expected to place the public's best interest ahead of their own self-interest. The U.S. Constitution refers in multiple places to "public Trust".[3] and to public offices being "of Trust.".[4] The Constitution also includes several provisions expressly designed to guard against self-interested decision-making..[5] Anti-conflict measures were much on the minds of the framers because, as James Madison explained in *The Federalist*:

> The aim of every political constitution is, or ought to be, first to obtain for rulers men who possess most wisdom to discern, and most virtue to pursue, the common good of the society; and in the next place, to take the most effectual precautions for keeping them virtuous whilst they continue to hold their public trust..[6]

Congress has built on this constitutional conception of a public office as a public trust across a wide range of federal ethics statutes, which employ a variety of mechanisms for keeping government officials "virtuous."

I will focus first on the executive branch. Financial conflicts of interest that could possibly bias an executive official's decision-making are addressed most directly in 18 U.S.C. § 208, a broad statute entitled "Acts Affecting a Personal Financial Interest." It prohibits any officer or employee of the executive branch (other than the president and vice-president) as well as any official or employee in an independent agency from participating "personally and substantially" in a "particular matter" having a direct and predictable effect on the financial interest of the employee, the employee's spouse or minor child, or on the financial interest of entities of which the official is a partner, director, or trustee. Section 208 thereby criminalizes conflicts created by personal investment holdings, even if the investment would be extremely unlikely to influence an officer or employee's official action. Executive branch officials have two alternatives: either recuse or divest whenever one's participation in a matter could implicate one's own financial self-interest, unless an exemption is available..[7] As the Supreme Court has

---

[3] U.S. CONST. art. VI, cl. 3.

[4] *Id.* art. I, § 3, cl. 7; *id.* art. I, § 9, cl. 8; *id.* art. II, § 1, cl. 2.

[5] *See, e.g.*, *id.* art. I, § 9, cl. 8 ("[N]o Person holding any Office of Profit or Trust under [the United States] shall, without the Consent of the Congress, accept any present, Emolument, Office, or Title, of any kind whatever, from any King, Prince, or foreign State."); *id.* art. I, § 6, cl. 2 (prohibiting Members of Congress from being appointed to a federal office that was created or that received an increase in salary during their time in Congress).

[6] THE FEDERALIST NO. 57 at 327 (James Madison).

[7] See Nagy, *Owning Stock While Making Law*, *supra* note 1, at 580 n. 71 (discussing the four exemptions in 18 U.S.C. § 208(b), which include a waiver issued by a supervisor after full disclosure of the possible

emphasized, the statute is "directed not only at dishonor, but also at conduct that tempts dishonor. . . .[It] is more concerned with what might have happened in a given situation than with what actually happened."[8]

Although there is not a single government-wide statute that requires executive officials to divest financial holdings in circumstances where the disqualification required under § 208 would fundamentally interfere with their government responsibilities, there are a host of agency-specific statutes that do require divestment. For example, Federal Communications Commission (FCC) employees are prohibited from holding financial interests in any company engaged in the business of radio or wire communication.[9] Moreover, agencies themselves have broad congressionally-granted authority to issue regulations prohibiting agency employees from specific categories of financial investments where such an interest "would cause a reasonable person to question the impartiality and objectivity with which agency programs are administered."[10]

Federal judges are likewise prohibited by a federal statute, 28 U.S.C § 455, from hearing any case or controversy in which their "impartiality might be reasonably questioned." The statute further mandates recusal when a justice or judge, or a spouse or minor child, has a financial interest in a case. Financial interest is defined broadly to encompass even a single share of stock in a party before the court or in a company substantially affected by the subject matter in controversy.[11]

For its own Members and most of its officers and employees, however, Congress has deemed prophylactic rules that guard against self-interested decision-making to be unwarranted. To be sure, both the Senate and House have ethics rules that prohibit Members (and employees and officers) from deriving personal financial benefits from the use of their official positions. But longstanding interpretations of those rules allow Members to work and vote on legislation impacting their own personal investments provided they are not the sole beneficiaries or part of an individualized class of beneficiaries. It is this sole beneficiary gloss that effectively insulates lawmakers from the loyalty obligations that would otherwise operate to restrict their personal investment practices. Indeed, the fiduciary duty of loyalty has both an anti-conflict component and an avoidance component, and the latter prohibits fiduciaries unable to recuse from "putting themselves in a position where, because of conflict or other concerns, they could

conflict, and the Office of Government Ethics adoption of a de minimis exception for holdings in an issuer's stock valued at $15,000 or less).

[8] United States v. Mississippi Valley Generating Co., 364 U.S. 520, 549-50 (1961).

[9] 47 U.S.C. § 154(b)(2)(A)(ii).

[10] 5 C.F.R. § 2635.403(a).

[11] 28 U.S.C. § 455(d)(4). The statute also makes clear that federal justices and judges have a duty to inform themselves about their personal financial interests and those of their spouse and minor children. *Id.* § 455(c).

not act on behalf of the beneficiary.”.[12] Thus, as Congress has rationalized, stock-investment conflicts need not be avoided because legislation that impacts publicly traded companies and industries almost by definition also affects thousands and sometimes millions of investors.

Consider first House Rule 3, which provides that Members should not vote if they have “a direct personal or pecuniary interest” in the legislation at hand..[13] The theoretical breadth of this provision has been practically undercut by House precedents emphasizing that financial interests are disqualifying only when a member’s vote affects him or her directly as an individual and not merely as one of a class. Accordingly, the House Ethics Manual observes that “[a]s a general matter. . . Members and employees need not divest themselves of assets upon assuming their positions, nor must Members disqualify themselves from voting on issues that generally affect their personal financial interests.”.[14] The Manual also makes clear that “[n]o federal statute, regulation, or rule of the House absolutely prohibits a member or House employee from holding assets that might conflict with or influence the performance of official duties.”.[15]

Senators are likewise prohibited from using their legislative power to advance their own personal interests. Rule 37(4) of the Senate Code of Official Conduct prohibits a Senator from knowingly using “his official position to introduce or aid the progress or passage of legislation, a *principal purpose* of which is to further *only* his pecuniary interest” or those of “his immediate family” or a “limited class” to which they belong. The Senate Ethics Manual aptly describes this prohibition as “narrow” and candidly acknowledges that “[l]egislation may have a significant financial effect on a Senator because his holdings are involved.”.[16] Yet, as long as the legislation “has a broad, general impact on his state or the nation,” Rule 37(4) does not prevent Senators “from voting on the legislation or playing an active role in advancing or blocking its passage.”.[17] The Manual goes so far as to convey an “*understanding* that the votes cast by Senators and Congressman are predicated on their perceptions of the public interest and the public

[12] Kathleen Clark, *Do We Have Enough Ethics in Government Yet?: An Answer from Fiduciary Theory*, 1996 U. Ill. L. Rev. 57, 71 (1996).

[13] CONSTITUTION, JEFFERSON'S MANUAL, AND RULES OF THE HOUSE OF REPRESENTATIVES, H.R. Doc. No. 112-161, at 934-35 (2013). Rule 23(3) of the House Code of Official Conduct likewise provides that Members “may not receive compensation and may not permit compensation to accrue to the beneficial interest of such individual from any source, the receipt of which would occur by virtue of influence improperly exerted from the position of such individual in Congress.”

[14] H. COMM. ON STANDARDS OF OFFICIAL CONDUCT, 110TH CONG., HOUSE ETHICS MANUAL at 247 (2008).

[15] *Id.* at 248.

[16] STAFF OF S. SELECT COMM. ON ETHICS, 108TH CONG., SENATE ETHICS MANUAL at 69 (COMM. PRINT 2003)

[17] *Id.*

good, not on personal pecuniary interest.”.[18] It is particularly peculiar for an *ethics manual* to include such a presumption.

The Senate Ethics Manual’s presumption of virtuous decision-making, however, is not carried forward to most staff employed by Senate Committees. That is, Senate Rule 37(7), enacted in 1977, requires a committee staff employee “to divest himself of any substantial holdings which may be directly affected by the actions of the committee for which he works” unless given written permission by the Ethics Committee to retain such holdings..[19] This disparate treatment is said to be justified because “committee staff members hold positions of responsibility” but “unlike Senators, committee staff are not publicly accountable, and despite public financial disclosure, their affairs are unlikely to get the same kind of scrutiny from the public and the press as Senators.”.[20]

Members of Congress have taken full advantage of the ethics rules and norms that currently function, at least with respect to stocks in publicly traded companies, as safe harbors for their personal investments. The result is that despite all the harsh media attention and Congress’s dismal public approval ratings, lawmakers continue to own and actively trade securities totaling hundreds of millions of dollars in companies directly impacted by legislative actions. Beyond that, the membership of many congressional committees holds disproportionately large investments in the industries subject to their oversight. The lack of parity among the three branches of government underscores the urgent need for legislative reform.

III. Public Disclosure of Personal Investments and the Discipline of the Electoral Process Do Not Constitute Effective Conflict-of-Interest Restraints

In the past, it has been the public’s interest in democratic representation that has been used, quite ironically, to justify Congress’s casual tolerance of its Members’ financial conflicts. That is, it is frequently emphasized that the citizens of this country are “entitled to have their elected representatives represent them by voting and fully participating in all aspect of the legislative process.”.[21] Recusal of potentially self-interested decision-makers, which is an anti-conflict mechanism often utilized by executive branch officials and federal judges, is therefore eschewed as an acceptable alternative for eliminating the self-interest that could arise from the holdings in a lawmaker’s investment portfolio.

---

[18] *Id.*

[19] Senate Rule 37, § 7, reprinted in SENATE ETHICS MANUAL at 322. The rule applies to committee staff earning more than “$25,000 per annum and employed for more than ninety days in a calendar year.” *Id.*

[20] S. SPECIAL COMM. ON OFFICIAL CONDUCT, SENATE CODE OF OFFICIAL CONDUCT, S. REP. NO. 95-49, at 44 (1977)

[21] SENATE ETHICS MANUAL at 69.

Notably, the House Ethics Manual expressly raises the divestment alternative to recusal and describes the divestment requirement as "impractical" and "unreasonable.".[22] It explains:

> Members of Congress enter public service owning assets and having private investment interests like other citizens. Members should not "be expected to fully strip themselves of worldly goods." Even a selective divestiture of potentially conflicting assets could raise problems for a legislator. Unlike many officials in the executive branch, who are concerned with administration and regulation in a narrow area, a Member of Congress must exercise judgment concerning legislation across the entire spectrum of business and economic endeavors. Requiring divestiture may also insulate legislators from the personal and economic interests held by their constituencies, or society in general, in governmental decisions and policy..[23]

But particularly in the context of today's lawmakers and their current financial investments, each of the above concerns regarding conflict avoidance through divestment rings hollow. First, a prohibition against holding securities in publicly traded companies would allow lawmakers to possess "worldly goods" in the form of shares in diversified investment funds that are widely held as well as in government securities. Moreover, while lawmakers may function as generalists when casting floor votes on a bill, much discretionary decision-making occurs at the committee level, where lawmakers function much more as specialists, charged with overseeing particular industries. And rather than "insulating" lawmakers from their constituents' interests, in view of the sliver of the public that owns stock in individual companies, permissible investment alternatives such as diversified mutual and index funds and Treasury securities would align constituent and member interests to a substantially greater degree.

With the divestment restraint dismissed largely through mistaken hyperbole, it is no wonder that the House Ethics Manual continues to reflect a conclusion that lawmakers' "conflicts of interest are *best* deterred through disclosure and the discipline of the electoral process.".[24] Yet, while that conclusion may have been worthy of credence four decades ago in the wake of the enhanced ownership disclosures mandated by the Ethics in Government Act of 1978,.[25] and while the STOCK Act's enhanced transaction-reporting requirements may have fueled some new justifiable hope in 2012,.[26] it is now

---

[22] HOUSE ETHICS MANUAL at 250.

[23] *Id.*

[24] HOUSE ETHICS MANUAL at 251 (emphasis added) (quoting HOUSE COMM'N ON ADMIN. REVIEW, FINANCIAL ETHICS, H. DOC. 95-73, at 9 (1977)).

[25] See *id.*, H. DOC. 95-73, at 9 (expressing the Commission's belief that disclosure and electoral discipline were the best approaches to conflicts "in the case of investment income").

[26] See 158 Cong. Rec. S309 (daily ed. Feb. 2, 2012) (statement of Senator Joseph Lieberman opposing an amendment to the STOCK Act that would have required divestment of individual stocks, and arguing the

clear that the increased transparency has not, in fact, sufficiently deterred lawmakers from owning and trading stock in companies subject to their oversight. If anything, it has made the problem worse because, thanks to journalists and good-government groups, the American public now sees even more quickly how frequently and extensively some lawmakers are benefitting from their own legislative activity.

Although there have been some recent and high-profile exceptions, Members' constituencies have proven to be quite tolerant (at least at the ballot box) even in instances where a member's glaring conflicts of interest were evident. Incumbents in Congress clearly "have an advantage over anyone who challenges their authority.".[27]

Moreover, as a leading political science scholar has pointed out, not only is "letting members disclose and voters decide" an ineffective approach in practice, it is also "deficient in principle" because it is grounded in a "mistaken view of democratic representation.".[28] Whereas a lawmaker's self-interested legislative activity can affect the entire country, only voters in that representative's district or a senator's state actually have a say in whether financial conflicts of interest are troubling enough to warrant an electoral defeat..[29]

IV. Notwithstanding the STOCK Act, Insider Trading Remains a Serious Concern That Would Dissipate if Congressional Officials are Prohibited From Owning Securities in Publicly Traded Companies

Illegal insider trading involves the use in securities trading of material nonpublic information that is misappropriated from the source of the information in violation of a relationship of trust and confidence. Government employees, like private-sector employees of banks, law firms, and corporations, often are entrusted with material nonpublic information and violate the law if they use this information for securities trading without first disclosing to their principals their intent to trade. Elected officials also are in a relationship of trust and confidence with the government and its citizens and can incur insider trading liability with respect to the material nonpublic information they learn in the performance of official duties. This point already should have been clear from the fiduciary character of federal office and the federal case law interpreting Section 10(b) of the Securities Exchange Act and Rule 10b-5. But to remove any doubt, Congress

---

public's increased "access to information about our holdings and our transactions . . . ought to be enough to guarantee the public . . . to make sure we are following the highest ethical norms").

[27] PAINTER, *supra* note 2, at 8-10.

[28] DENNIS F. THOMPSON, ETHICS IN CONGRESS: FROM INDIVIDUAL TO INSTITUTIONAL CORRUPTION at 137 (1995)

[29] See *id.* at 138 (emphasizing that "citizens rightly take an interest in the ethical conduct of all members, not only of their own representative").

enacted the STOCK Act, which amended the Securities Exchange Act to provide that a Member of Congress and any officer or employee "owes a duty arising from a relationship of trust and confidence to Congress, the United States Government, and the citizens of the United States with respect to material, nonpublic information derived from such person's position . . . or gained from the performance of such person's official responsibilities.".[30]

One of several difficulties with the application of insider trading law to congressional officials is that trading on the basis of material nonpublic government information will often be difficult to prove. Discerning whether a member of Congress or a staff member was in possession of such information requires trained investigators, probably from the Securities and Exchange Commission (SEC) or from the Department of Justice, to obtain copies of and review emails, phone logs, and testimony of witnesses who know what information was disclosed to the member and when. Such an investigation, among other issues, raises complicated issues under the Speech or Debate Clause of the Constitution,.[31] and even if constitutionally permissible is very likely to encounter strong pushback from congressional leadership.

There have been several high-profile instances of such pushback, and because the investigative phase of SEC and DOJ insider-trading investigations is generally confidential, there may well have been others. One of the most troubling instances began just 20 months after the enactment of the STOCK Act. The SEC in early 2014 sought documents from the House Ways and Means Committee as well as documents and testimony from a former staff director of the Committee's health subcommittee. The staff director was suspected of possibly tipping a so-called political intelligence consultant about yet-to-be announced changes in payment rates for physicians serving Medicare patients. But counsel for the House initially refused to cooperate voluntarily and then sought to block the SEC's investigatory subpoenas. One of the House's legal arguments was that the sovereign-immunity doctrine bars the enforcement of an inter-branch subpoena. Its other key argument was that the information sought in the insider-trading investigation was protected by the Speech or Debate Clause. Although the federal district judge ruled partially in the SEC's favor,.[32] the litigation continued as House counsel

---

[30] Section 21A(g) of the Securities Exchange Act, 15 U.S.C. § 78u-1(g).

[31] Article I, Section 6, Clause 1 of the Constitution provides that Members of Congress "shall in all Cases, except Treason, Felony and Breach of the Peace be privileged from Arrest during their attendance at the Session of their Respective Houses, and in going to and from the same; and for any Speech or Debate in either House, they shall not be questioned in any other Place."

[32] See SEC v. House Committee on Ways and Means and Brian Sutter, 161 F.Supp.3d 199 (S.D.N.Y. 2015) (ruling against the sovereign-immunity claim, but holding that certain sought-after documents and aspects of testimony were within the "sphere of legitimate legislative authority" and thus fell within the Speech or Debate Clause's protection).

appealed to the Second Circuit. The dispute was not resolved until nearly three years from the start of the SEC's investigation, when the parties announced their stipulation "to seek the dismissal of the appeal.".[33] It is hardly surprising that, in the view of some, the practical and constitutional hurdles involved in a congressional insider-trading investigation "make prosecution impossible for [trading based on] certain types of information received officially in committee or other legislative settings.".[34]

Another consequence of the operation of federal insider trading law is that congressional officials who own securities in individual companies, when confronted with a conflict of interest, also may not be able to sell the securities to resolve the conflict without risking liability for a violation of Section 10(b) and Rule 10b-5 of the Exchange Act. If material nonpublic information is disclosed to officials at the time they become aware of a conflict of interest, it may be too late to sell the securities and recusal may be the only option that is both legal and ethical.

Many of these insider-trading problems would be avoided if the Member or senior staff person did not own securities in publicly traded companies to begin with. Given the wide range of matters that come before Congress, and in view of Congress's increasing involvement with financial markets and private-sector businesses (such as banks, health care/providers, and automobile manufacturers), this reason is yet another one for Members to divest of individual stocks and certain other investments upon entering Congress and to remain divested until they depart.

****

I will conclude by emphasizing how appearances alone can foster corrosive beliefs that personal financial interests are routinely placed ahead of the public interest. Even if Members of Congress are not influenced by personal finances in sponsoring bills or casting votes, ownership of securities affected by legislation creates the appearance of corruption. And even if a Member does not trade on material nonpublic government information, the public may suspect otherwise. Such perceptions are typically magnified in election years when opponents feature allegations of financial conflicts and out-sized securities trading profits in attack ads. Instilling public confidence in Congress requires lawmakers to impose upon themselves certain prophylactic rules that guard against financial conflicts and reinforce obligations of loyalty and trust—and that should include

[33] See Martin O'Sullivan, *House, SEC Drop Health Care Subpoena Fight at 2d Circ.*, Law 360 (November 14, 2016).

[34] Stanley M. Brand, *DOJ Drops Investigation Into Three Senators for Insider Trading, Burr Probe Continues*, The Conversation (Apr. 2, 2020).

a federal statute prohibiting ownership of publicly traded securities as well as certain other financial investments that will likely conflict with official duties.

Today's hearing constitutes a monumental step toward bringing about real and profound change in the ethical norms and conflict-of-interest restraints that will apply to Congress. I am truly honored to be a part of it, I look forward to your questions, and I stand ready to be of whatever help I can as the legislative process progresses. Thank you very much.

The CHAIRPERSON. Thank you very much.

And now we have our final witness, Ms. Schulp. We will welcome your testimony for five minutes.

STATEMENT OF JENNIFER J. SCHULP

Ms. SCHULP. Thank you.

Chairperson Lofgren, Ranking Member Davis, and distinguished Members of the Committee on House Administration, my name is Jennifer Schulp, and I am the Director of Financial Regulation Studies at the Cato Institute's Center for Monetary and Financial Alternatives. Thank you for the opportunity to take part in today's hearing.

As you know, the questions raised by Members of Congress trading stocks are not new. A decade ago, the STOCK Act clarified the applicability of insider-trading prohibitions to lawmakers and required periodic disclosure of stock transactions, but concerns have persisted about lawmaker stock trading.

Although recent polling shows widespread public support for banning lawmakers from owning or trading stocks, such measures are too broad for preventing insider trading and too narrow to effectively address the question of financial conflicts of interest. Because financial conflicts of interest present complex tradeoffs not easily solved by a simple prohibition, it is better to focus on increasing transparency through disclosure.

Despite headlines to the contrary, there is little evidence that unlawful insider trading is widespread on Capitol Hill. Recent research looking at post-STOCK Act trading data has found that lawmakers do not reap outsized returns, including for investments in areas where lawmakers hold committee assignments. Yet questionable trading has fed a public perception that lawmakers have financial advantages.

Analyzing lawmakers' trading is more than fair and has been made possible in part by the STOCK Act's reporting requirements. But current law already delineates when such trading is unlawful. It does not follow that all stock ownership or trading should be prohibited just because no STOCK Act prosecutions have been brought. This is especially true where there is no evidence of widespread insider trading.

Moreover, taking prophylactic action to combat insider trading does not address the actual issue. There is reason to believe that those calling for congressional stock-trading reform are not motivated by a crisis of faith in the markets but, rather, a lack of trust in lawmakers. A focus solely on individual stocks distracts from the broader issue, that the public perceives lawmakers to be using their positions for financial gain.

Members of Congress are uniquely positioned to not only have access to information impacting stock values but also the ability to influence those values directly and indirectly. But this complication exists not only for individual stocks but for mutual funds, exchange-traded funds, crypto holdings, business interests, and other financial interests. Individual stock restrictions address only a narrow portion of these potential conflicts and, as such, may do little in the long term to enhance voters' trust in Congress.

The question, then, is how to manage this multitude of potential conflicts. While it is tempting to say that conflicts should be eliminated, this solution is not practical across the range of potential financial conflicts of interest that lawmakers face.

Importantly, seeking to eliminate a particular conflict, such as trading in individual stocks, may have unintended effects on the quality of representation that voters receive, either by discouraging some from running for office or by decreasing the connectedness between Representatives and the impact of their decisions.

Disclosure provides a more complete solution, bringing the conduct of lawmakers into the light, discouraging questionable trading, and providing voters with information about the conflicts of interest that their Representatives face.

The STOCK Act provides a good foundation for this transparency, but it has fallen short of its potential, and enhancements should be considered to provide additional transparency.

The first place to focus is on ensuring that penalties for noncompliance are consistently applied. It is worth examining whether the penalty framework is sufficiently deterrent and considering public reporting of delinquent disclosure. It is also worth considering whether aspects of reporting can be automated to ease compliance burdens.

Second, the disclosure requirements themselves could be improved—for example, by shortening the long lag between the execution of a trade and the deadline for disclosure.

Enhancing transparency permits voters to choose whether the conflicts faced by their elected Representatives are problematic even if the trading itself is perfectly legal. Empowering voters with information limits unintended consequences of restrictions and puts the choice in the hands of voters, where it belongs.

Thank you, and I welcome any questions that you may have.

[The statement of Ms. Schulp follows:]

CATO INSTITUTE | Center for Monetary and Financial Alternatives

Testimony
Before the Committee on House Administration
Hearing on "Examining Stock Trading Reforms for Congress"

Jennifer J. Schulp
Director of Financial Regulation Studies
Center for Monetary and Financial Alternatives, Cato Institute

April 7, 2022

Chairperson Lofgren, Ranking Member Davis, and distinguished members of the Committee on House Administration, my name is Jennifer Schulp, and I am the Director of Financial Regulation Studies at the Cato Institute's Center for Monetary and Financial Alternatives.

I thank you for the opportunity to take part in today's hearing entitled, "Examining Stock Trading Reforms for Congress."

As you know, the questions raised by members of Congress trading stocks are not new. They were most recently addressed by the STOCK Act in 2012,[1] as amended in 2013, which clarified the applicability of insider trading prohibitions to lawmakers and required periodic disclosure of stock transactions. Despite the passage of that Act, concerns have persisted about the stock trading activities of lawmakers, including some trading during the COVID-19 pandemic that has drawn both public scrutiny and governmental investigations. In response, many have questioned whether members of Congress should be subject to further restrictions on their abilities to hold or trade stocks.

Despite recent polling that shows widespread public support for banning lawmakers from owning or trading individual stocks,[2] these measures are not justified to prevent insider trading by members of Congress and fail to consider the broader question of addressing conflicts of interest that is necessary to increase the public's trust in Congress. Because financial conflicts of interest present complex tradeoffs—not easily solved by a simple prohibition on

[1] Stop Trading on Congressional Knowledge Act of 2012 (STOCK Act), Pub. L. No. 112-105, 126 Stat. 291 (2012).
[2] Data for Progress, available at https://www.filesforprogress.org/datasets/2021/2/dfp_feb_21_congress_stocks_toplines.pdf; Karl Evers-Hillstrom, "Three in four vote support banning lawmakers from trading stocks: poll," The Hill (January 6, 2022), available at https://thehill.com/homenews/news/588630-76-percent-of-voters-support-banning-lawmakers-from-trading-stocks-poll; Claire Williams, "Most Voters of All Parties Support Congressional Stock Trading Restrictions," Morning Consult (January 19, 2022), available at https://morningconsult.com/2022/01/19/ban-stock-trading-congress-poll/.

conduct—the better focus is on increasing transparency. In this way, the STOCK Act laid the correct foundation of disclosure for both discouraging legally questionable trading and providing voters with important information about the potential and actual conflicts of interest that their elected representatives face.

New Restrictions Are an Unnecessarily Broad Solution to Prevent Insider Trading

The STOCK Act made clear that members of Congress could be subject to insider trading liability for trading on material, non-public information learned from a member's official duties.[3] Preventing such insider trading has been widely invoked today as a reason for prophylactically banning lawmakers from owning or trading individual stocks. But such measures are not tailored to address a problem that already has legal remedies, and such broad restrictions have the potential to themselves create other negative consequences.

To begin, despite headlines to the contrary, there is little evidence that unlawful insider trading is widespread on Capitol Hill. Recent research has found that lawmakers reap no particular outsized return on their stock investments, including for investments made in areas where lawmakers hold committee assignments.[4] Research finding that there is a congressional advantage in trading tends to draw on pre-STOCK Act trading data[5] or to present anecdotal conclusions.[6]

It is true that even in the absence of this evidence, there is a public perception fed by questionable trading that members of Congress may be using information to trade for their own financial advantage. Questioning lawmakers' trading is more than fair, and has been made possible, in part, by the STOCK Act's reporting requirements. But determining whether such trading is unlawful is already contemplated by existing law. Just because no insider trading prosecutions have been brought against lawmakers under the STOCK Act's provisions since its enactment—or that prosecuting insider trading violations by members of Congress is

---

[3] STOCK Act, § 3; 15 U.S.C. § 78u-1(g).

[4] William Belmont, Bruce Sacerdote, Ranjan Sehgal and Ian Van Hoek, "Relief Rally: Senators As Feckless As the Rest of Us at Stock Picking," National Bureau of Economic Research Working Paper 26975 (April 2020), available at https://www.nber.org/papers/w26975; William Belmont, Bruce Sacerdote, Ranjan Sehgal and Ian Van Hoek , "Do senators and house members beat the stock market? Evidence from the STOCK Act," Journal of Public Economics 207 (2022). These studies examine trading between 2012 and 2020, and find no superior investment performance for members of Congress. These studies are consistent with a study examining pre-STOCK Act trading. Andrew C. Eggers and Jens Hainmueller, "Capitol Losses: The Mediocre Performance of Congressional Stock Portfolios, 2004-2008," The Journal of Politics, Vol. 75, No. 2 (April 2013), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1762019.

[5] Serkan Karadas, "Trading on Private Information: Evidence from Members of Congress" (2015), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2712297. This study uses a data set of congressional trading from 2004-2010, prior to the STOCK Act, to conclude that the performance of congressional portfolios is driven by private information acquired by lawmakers.

[6] Unusual Whales, "Congressional Trading in 2021," available at https://unusualwhales.com/i_am_the_senate/full. While this type of analysis may be useful for providing voters with information about their elected representatives, it is not rigorous analysis of whether insider trading occurs, or is widespread, among lawmakers.

challenging for a number of reasons[7]— it does not follow that their stock ownership or trading should be prohibited, especially where there is no evidence that potential violations of the law are widespread.

Moreover, limiting the flow of information to the market from any particular subset of traders has the potential to harm market efficiency.[8] Prohibitions on insider trading already have this effect by preventing a stock's price from reflecting all of the information known about the stock. A broad-based ban on stock trading or ownership could add to that inefficiency by preventing lawmakers' trades from contributing information that allows the markets to engage in price discovery. Because the type of information that members of Congress are privy to relates not just to individual companies, but to entire industries and the whole economy, it would be desirable for such information to be absorbed quickly into the market, rather than kept out—particularly when doing so does not violate existing insider trading law.

Finally, and perhaps most importantly, a stock ownership or trading ban enacted to prevent insider trading by members of Congress does not appear to address the actual problem faced by legislators. The Securities and Exchange Commission (SEC) considers insider trading to "undermine investor confidence in the fairness and integrity of the securities markets."[9] But, there is reason to believe that the public polling calling for congressional stock trading reform does not indicate a crisis of faith in the markets, but rather indicates a lack of trust in lawmakers.[10] That issue requires a different—and wider—frame of reference for considering policy solutions.

New Restrictions Are a Poor Solution for Addressing Existing Conflicts of Interest

Focusing solely on the question of trading or owning individual stocks obscures the broader questions of preventing lawmakers from using their positions for personal, financial gain and combatting the public perception that lawmakers are doing so. This task is complicated by the fact that members of Congress are uniquely positioned: they have access to information that may impact the value of particular stocks, and they have the ability to impact

[7] Robert Anello, "How Senators May Have Avoided Insider Trading Charges," Forbes (May 26, 2020), available at https://www.forbes.com/sites/insider/2020/05/26/how-senators-may-have-avoided-insider-trading-charges/?sh=5c9e238e27ba.

[8] *See, e.g.*, Henry G. Manne, "Insider Trading: Hayek, Virtual Markets, and the Dog that Did Not Bark," Journal of Corporation Law, Vol. 31, No. 1 (Fall 2005), available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=679662.

[9] U.S. Securities and Exchange Commission, Investor.gov, "Insider Trading," available at https://www.investor.gov/introduction-investing/investing-basics/glossary/insider-trading.

[10] Congressional Job Approval, RealClearPolitics, available at https://www.realclearpolitics.com/epolls/other/congressional_job_approval903.html (showing a composite job approval for Congress at 21%); Pew Research Center, "Public Trust in Government: 1958-2021," available at https://www.pewresearch.org/politics/2021/05/17/public-trust-in-government-1958-2021/ (finding only 24% of respondents in April 2021 trust government to do what is right just about always or most of the time).

the value of particular stock themselves by legislating, calling for investigations, or otherwise exerting their political influence.

These potential conflicts of interest can exist not only in a lawmaker's ownership of individual stocks, but also in their ownership of mutual funds and exchange traded funds, their crypto holdings, and their business interests, among other places. Indeed, a very similar potential for personal enrichment exists with respect to holdings in investment funds that track the performance of other assets, regardless of the diversification of those funds, because lawmakers are privy to information that affects more than just individual companies. Importantly, these conflicts of interest are not limited to the lawmaker alone but may arise through the interests of their families and staff. Restricting a lawmaker's abilities to own or trade individual stocks addresses only a narrow portion of these potential conflicts and, as such, may do little in the long-term to enhance voters' trust in Congress.

The question, then, is how to manage this multitude of potential conflicts. The overarching framework to addressing this question is the Ethics in Government Act.[11] While this framework does restrict some lawmaker conduct, the primary method employed is disclosure. To that end, lawmakers are subject to extensive financial disclosure requirements, including annual disclosures about their assets, liabilities, and income.[12] The STOCK Act's disclosure requirements supplement these annual disclosures by requiring periodic disclosure of certain financial transactions in stocks, bonds, commodities, futures, and other securities. Given the interrelationship between stock holdings and other financial interests, and the similar conflicts presented by each, stock holdings should be subject to the same method of conflict mitigation as other financial interests.

While it is tempting to conclude that the only way to manage a conflict of interest is to eliminate it, such a solution is impractical when looking at the range of potential financial conflicts of interest that lawmakers face. Moreover, seeking to eliminate a particular conflict—such as trading in individual stocks—may have wider effects on the quality of representation that voters receive, either by discouraging some from running for elected office or by decreasing the connections between representatives and the impact of the decisions that they are making.

Transparency Best Balances the Interests of Voters

Instead of relying on prohibitions, which are incomplete and may have unintended consequences, disclosures bring the conduct of lawmakers into the light, permitting judgment by both the voters who grant them their positions and those tasked with enforcing the laws.

---

[11] 5 U.S.C. §101, *et seq.*

[12] U.S. House of Representatives Committee on Ethics, Instruction Guide Financial Disclosure Statements and Periodic Transaction Reports (2020), available at https://ethics.house.gov/sites/ethics.house.gov/files/documents/CY%202020%20Instruction%20Guide%20for%20Financial%20Disclosure%20Statements%20and%20PTRs.pdf.

The STOCK Act provides a good foundation for this transparency. In fact, watchdog groups have aggregated this information in user friendly formats for voters and others to use.[13]

The STOCK Act, however, has fallen short of its potential in some respects. As has been widely reported, lawmakers have a poor record in complying with the trade reporting requirements,[14] and penalties for non-compliance have been inconsistently applied.[15]

It is premature to declare the disclosure regime of the STOCK Act insufficient when it has not been consistently enforced. Options should be considered for increasing compliance with the STOCK Act's disclosure requirements, including ensuring the consistency of penalties for noncompliance. The level and structure of penalties should also be revisited to ensure that penalties are sufficient to provide a deterrent effect to discourage noncompliance. Given technological improvements since the STOCK Act was passed, it is worth considering whether aspects of reporting can be automated, easing both submission by lawmakers and review for compliance with the requirements.

It is also worth revising the disclosure requirements of the STOCK Act to determine whether additional transparency is desirable and feasible. For example, there currently is a long lag between the execution of a trade and the deadline for disclosure: 30 days after the transaction or no more than 45 days after the trade if the lawmaker did not become aware of the trade when executed. Lawmakers are given a 30-day grace period beyond those generous time periods before which their submission is determined to be non-compliant. The grace period itself seems to be at odds with timely reporting, but even the required reporting periods are multiple times longer than required by the SEC for trade reporting by public company insiders.[16] Shortening the time for reporting would provide additional transparency.

It is also worth considering whether additional transparency should be provided with respect to lawmaker non-compliance. Publicly reporting when disclosure was not filed in a timely manner and when a lawmaker was penalized for such deficiencies can provide information to voters as to whether their elected representatives are meeting their disclosure obligations.

---

[13] A number of websites track this information, including Capitol Trades (https://www.capitoltrades.com/), House Stock Watcher (https://housestockwatcher.com/), Senate Stock Watcher (https://senatestockwatcher.com/), among others.

[14] Dave Levinthal, "57 members of Congress have violated a law designed to stop insider trading and prevent conflicts-of-interest," Business Insider (March 3, 2022), available at https://www.businessinsider.com/congress-stock-act-violations-senate-house-trading-2021-9.

[15] Camila DeChalus, Kimberly Leonard, and Dave Levinthal, "Congress and top Capitol Hill staff have violated the STOCK Act hundreds of times. But the consequences are minimal, inconsistent, and not recorded publicly," Business Insider (December 15, 2021), available at https://www.businessinsider.com/congress-stock-act-violations-penalties-consequences-2021-12.

[16] By way of comparison, corporate insiders must report trades to the SEC within two business days. *See* Securities and Exchange Commission, Insider Transactions and Forms 3, 4, and 5, available at https://www.sec.gov/files/forms-3-4-5.pdf.

Enhancing transparency permits voters to choose whether the conflicts faced by their elected representatives are problematic, even if those trades are perfectly legal. Providing voters with the information to make those choices limits unintended consequences of additional restrictions and puts the choices in the hands of the voters, where they belong.

* * *

Thank you for the opportunity to provide this information, and I welcome any questions that you may have.

The CHAIRPERSON. Thank you very much.

And thanks to each one of our witnesses for very useful testimony.

This is the time when Members can address the witnesses with questions. Mr. Steil is recognized, at the request of the Ranking Member, to go first for five minutes.

Mr. STEIL. Thank you very much, Madam Chairperson. We have conflicting hearings today, and so I appreciate your willingness to let me jump in.

I think where we maybe should begin is: One, what is legal and illegal under current law? And two, what are the priorities and objectives and goals of putting forth this framework?

And so, as I look at this—and, Ms. Schulp, I would love for you to comment on this—it is to facilitate compliance with the law. Under, current law, insider trading is illegal, including for Members of Congress. We can have a conversation about the enforcement of that. Using information derived from one's position here in Congress is illegal under current law. We could have a conversation about enforcement mechanisms of that.

And so, compliance with the law I think is a key principle that we should be looking at. Ensuring Members' family and staff don't take unfair advantage of information gained from their congressional work I think is an important topic for us to consider as we look at this. And to provide confidence to the American people that we follow that, that we avoid the appearance of an impropriety. I think those are key principles, amongst others.

Are there other key principles that you think that we should consider before I begin my questioning here?

Ms. SCHULP. Yes, I believe that those are the key principles here. You are correct——

Mr. STEIL. Okay.

Ms. SCHULP [continuing]. That insider trading is already illegal.

Mr. STEIL. Okay. So, then, let's dive in.

We have heard a series of ways that we can enhance this to make sure that we are avoiding the appearance of impropriety, that we enforce the law, and we make sure that Members follow that law.

Let's dive in first to the blind trust. Would the blind—first, what are the compliance costs as it relates to a blind trust? What would be the compliance costs for Members in a blind trust scenario?

Ms. SCHULP. Compliance costs for blind trusts tend to be substantial. Usually, it takes multiple thousands of dollars to set one up, and——

Mr. STEIL. Okay. So——

Ms. SCHULP [continuing]. There is an ongoing——

Mr. STEIL. No, no. I am just going to move quickly because I am limited on time.

So, it is substantial. We could decide whether that is good or bad, but it is a substantial cost.

And then would the public have confidence in the execution of the blind trust? Meaning, a blind trust is only as good as it is blind. Is that a fair assessment?

Ms. SCHULP. That is a fair assessment.

Mr. STEIL. So, the structure of that blind trust, then, becomes paramount if Congress chose to go down that path.

Let's shift gears: a complete stock trading ban, thinking about the implementation of that. So, envision a Member of Congress coming here. Say she was previously an executive at a publicly traded company; she has a significant portfolio. Would she then be required to divest that entire portfolio upon arrival in Congress?

Ms. SCHULP. Some of the proposals would require that.

Mr. STEIL. And what would happen if somebody had to fully divest—if she had to fully divest her portfolio, what would be the general implications to her?

Ms. SCHULP. The first is that there could be substantial tax consequences for that. And, depending on where the market is, there could be substantial losses to her investment.

Mr. STEIL. Or substantial gains, but——

Ms. SCHULP. Yes.

Mr. STEIL [continuing]. Substantial tax implications for her upon arrival. That may be a consideration as to whether she chooses to run in the first place.

I think something worthwhile for us to consider is how we would begin that implementation for somebody who arrives in that capacity.

Let me shift gears slightly for something I don't think we have talked a ton about. I used to work at a publicly traded company. I was involved in the enforcement of section 16(a)—officers, their compliance with securities laws. Our securities laws give us a framework with which to understand how publicly traded companies deal with this insider information, the appearance of impropriety for those insiders as well.

Do you think that Members should be banned from what I am going to call sophisticated trades—swaps, options, shorting stocks? Would that improve individual—would that improve the public's confidence that Members are not engaging in insider trading?

Ms. SCHULP. No. I think it will have little difference on the public's confidence on that front.

Mr. STEIL. Okay. I may or may—I may not fully agree with that. I think there are some opportunities that we may want to consider and look at in that space.

Let me shift gears, then: in particular, with other ways of adjusting the protocols to accomplish the same benefit without maybe a full ban of stock, just to explore this space. Would minimum holding periods improve the public's confidence in Members of Congress abiding by the law?

Ms. SCHULP. It may have some effect.

Mr. STEIL. So, if you had a—say, just for the sake of throwing a number out, if you had a ninety-day minimum holding period, or remove quick movements in and out of stocks, it would be longer than the duration of a publicly traded company's financing reporting, it may improve the confidence of the American people in Members?

Ms. SCHULP. There may be some effect in that.

Mr. STEIL. May be worth us considering that.

The other is our current regime has a disclosure after the sale of stock. Some public companies have gone forward with a disclosure prior to the sale or acquisition—a delayed closing, if you will, let's say for sake of discussion ten days, where an announcement would be made ten days in advance, prior to the sale or acquisition of a stock.

Would that alter the appearance of the impropriety as people would be analyzing a Member of Congress or another insider from engaging in a trade?

Ms. SCHULP. It may have some effect.

Mr. STEIL. And would the burden placed upon that Member, or a spouse be significant or lighter than a blind trust scenario or a forced sale?

Ms. SCHULP. It should be lighter than a blind trust or a forced sale.

Mr. STEIL. I appreciate your insights today.

Cognizant of the time, Madam Chairperson, I yield back.

The CHAIRPERSON. The gentleman yields back.

Mr. Butterfield is recognized for five minutes.

Mr. BUTTERFIELD. Thank you very much, Madam Chairperson. And thank you for convening this very, very important hearing today.

I especially want to thank the five witnesses for your testimony as well.

Mr. Sherman, it is good to see you again.

Mr. SHERMAN. Good to see you again, sir.

Mr. BUTTERFIELD. I was on the Ethics Committee when you served as counsel to the Ethics Committee, and it looks like you have landed well. I just want to thank you for your many years of service.

Madam Chairperson, you were the Chairperson of the Ethics Committee when I was there.

The CHAIRPERSON. That is correct.

Mr. BUTTERFIELD. I will say publicly that, out of the eighteen years that I served in Congress, those two years or four years on the Ethics Committee were the worst years of my life.

The CHAIRPERSON. I don't take it personally because I concur.

Mr. BUTTERFIELD. And it had nothing to do with you, Madam Chairperson nor you, Mr. Sherman.

I had spent thirty years in a courtroom before coming to Congress, and, you know, in a courtroom, the rules are so much different than the rules for ethics for Members of Congress. One, for example, there is a presumption of guilt. I don't know if Members fully know that or appreciate it if you have not been confronted with an ethics violation, but there is a presumption of guilt. The burden of proof is on the Member to prove that she is not guilty of the offense for which she is charged. And that was just so, so different from what I had been exposed to in a courtroom.

The final thing that I found very interesting was that a Member's failure to cooperate with the process was deemed to be a violation of the ethics rules.

And so, when I say those were some very difficult years, they were.

But while I am with you, Mr. Sherman, let me just start with you. You have testified that your organization recommends a legislative proposal that requires a comprehensive ban on both trading and ownership of individual stocks and other securities by Members and their spouses and dependents.

So, my question to you—and I have great respect for CREW—what is CREW's perspective of the various legislative proposals that ban stock trading but permit stock ownership through the use of qualified blind trusts, which are currently allowed by law? I know you touched on it earlier, but if you would be a little bit more illuminating in your response.

Mr. SHERMAN. Absolutely. And thank you for the question.

I think the misnomer with respect to qualified blind trusts is that it only works if it is truly blind. Our position is that qualified blind trusts could be a useful option if the Member is required to effectuate the sale of all the assets that would go into that trust beforehand. Right? A trust can't be blind if the Member knows that they owned Microsoft the day before it went into the trust. They know that they still own it the day after.

Mr. BUTTERFIELD. Let's talk about judges. Half of my legal career, I was a judge back in North Carolina, and I have great interest in judicial service.

But does your organization have any recommendation for addressing the crisis of widespread recusal failure—failure to recuse—and lack of transparency regarding financial conflicts of interest in the Judicial Branch, in the Federal Judicial Branch?

Mr. SHERMAN. Absolutely. I agree with you that the conflict-of-interest issues that have arisen in the Federal judiciary and have been exposed through detailed reporting are a crisis of confidence and need to be addressed by the Congress.

I would note, though, that one distinction between the ethics regime that applies to the Federal judiciary versus Members of Congress is that recusal is an option. The problem with the Federal judiciary is that judges didn't recuse. Here in Congress, recusal is not a viable option for Members of Congress that have a financial conflict of interest, because it denies their constituents effective representation in this body.

Mr. BUTTERFIELD. Finally, Professor Nagy—I can't pronounce that exactly, but thank you for your service.

Ms. NAGY. Nagy.

Mr. BUTTERFIELD. Thank you for your testimony. Thank you for your testimony thirteen years ago or whenever you testified before the STOCK Act was passed.

Some people have argued that new prohibitions on stock-trading activity or ownership are unnecessary. Some are saying that. They are saying it because public disclosure and the electoral process should be enough; it should be sufficient to address conflicts of interest. They argue that disclosure allows for the public and good-government groups to track trading activity and assess whether elected officials have acted ethically and that, informed by those disclosures, voters can remove unethical lawmakers at the ballot box.

That seems extreme to me. What is your perspective on this argument?

Ms. NAGY. Well, my perspective is that, in 1978, Congress enacted the Ethics in Government Act with disclosure as the solution, or the proposed solution, for the conflicts of interest. Ten years ago, in the STOCK Act, we put in transparency reporting requirements where 45 days after—and disclosure hasn't worked.

If anything, disclosure of financial transactions puts it glaringly obvious to the public that the conflicts of interest are there.

The voters decide, let the voters and the ballot box decide—that reflects a misconception of the corrosiveness that conflicts of interest have. A——

Mr. BUTTERFIELD. Thank you.

Ms. NAGY [continuing]. Voter only in one district decides the answer for that Representative, but that Representative's conflicts affect us all.

Mr. BUTTERFIELD. I agree. Absolutely.

Thank you. I yield back.

The CHAIRPERSON. The gentleman yields back.

The Ranking Member is recognized for five minutes.

Mr. DAVIS. Thank you, Madam Chairperson.

This is a very interesting hearing. I appreciate all the witnesses' testimony.

I am hoping that some of the witnesses' testimony hasn't already led the majority to, kind of, assess what type of legislative proposal they are going to put forth. Because I think the discussion, we are having today is too important to not take a step back and understand where we are as an institution.

There is a common theme here, that corrupt people do corrupt things. Right? And we should make sure that corrupt people don't have an opportunity to do that.

Our goal also is to make sure that those who want to follow the law and those who want to follow transparency measures can do so without being labeled corrupt. That is our charge. Our charge is to develop something that makes the public comfortable that we, as Members of Congress, are transparent in what we do financially, but, at the same time, we are working through a prism of testimony that was based upon corrupt individuals.

Did any of you research our or log into our financial disclosure portal before you came here to testify today? Raise your hand if you did.

Okay. Any of you look at mine? Raise your hand if you did.

Nobody? Why wouldn't you? Why wouldn't you look at our disclosures, those of us who are questioning you?

Because if you did, you would see that I don't trade a lot of stocks. I got my only individual stock holding when I was a child because my father happened to work as a franchisee for a corporation called McDonald's. I haven't traded that stock since I got here. My kids, my dependent children have that same asset. You know one reason I don't trade it? Because I don't want to go through the paperwork of the STOCK Act reporting requirements.

However, because I have owned this stock since I was a child, much of your testimony says that maybe I should sell it, right?

Now, since I own that one stock—Mr. Sherman, I have a question for you. I was really interested in the comment that you said, that, you know, owning and trading individual securities undermines the critical work of the entire Federal Government. Does my owning an individual stock since my childhood undermine the credibility of the Federal Government?

Mr. SHERMAN. I think it is reasonable for any constituent to question whether their Member's stock ownership——

Mr. DAVIS. They can do that at the ballot box.

Mr. SHERMAN [continuing]. Has an impact on——

Mr. DAVIS. I want to reclaim my time——

Mr. SHERMAN [continuing]. Their legislative work.

Mr. DAVIS. I am going to reclaim my time really quick, because I want to go a little further on this.

Mr. SHERMAN. Sure.

Mr. DAVIS. So, now that I am a Member of Congress and I own that one stock—my dependent children own similar stock that they were gifted. My wife does not. So, if I go to, let's say, a McDonald's restaurant—because that is the only stock that I have owned since a child—and buy lunch, is that something that is unethical?

Mr. SHERMAN. Certainly not.

I think we need to craft ethics policy around the concept of, one, public service is a public trust. And we need to design a policy that would give the public the greatest confidence that their elected Representatives and the body does not have financial conflicts of interest and that Members aren't acting on them.

Mr. DAVIS. Well, it took me about two minutes to find my disclosure. I would urge you all to go in and find out if any of us here have any so-called conflicts of interest. Because we need a baseline—we need a baseline of what all of you experts think would be a conflict of interest. Because, I mean, we think we are complying with all the rules and requirements that we need.

Ms. Nagy, I am interested in your testimony. You talked about the placement of—you testified, the placement of accumulated assets into QBTs, qualified blind trusts, is only a minimally effective anti-conflict measure.

How much does it normally take to have a financial company offer you a blind trust? Don't they have minimums——

Ms. NAGY. They do.

Mr. DAVIS [continuing]. Minimum investments? What are they?

Ms. NAGY. I think it varies according to the financial companies, but it's a significant amount of assets.

Mr. DAVIS. It is a significant amount.

My wife—because her financial advisor is a friend of ours and because of our reporting requirements, he is not allowed to change any investments in her mutual funds on any given year, because it is very difficult to comply, and we want to be sure—we want to do the right thing here.

But I asked my financial advisor, her financial advisor, how much the minimum amount would be. You can go look at how many stocks I own—which, again, is one—and I am nowhere near the minimal amount for a $500,000 minimum investment to create a qualified blind trust.

Were you all aware of those limitations? Do you know how many Members of Congress would have that amount of money to put into a qualified blind trust? Anyone?

Ms. HEMPOWICZ. May I respond?

Mr. DAVIS. Sure.

Ms. HEMPOWICZ. Yes. I think it is important to remember, when we are talking about blinds trusts, that I don't think any of the legislation that is in front of Congress would force a Member to take advantage of the blind trust. Therein, the option is given to Members who would choose not to divest.

We see that same structure in the executive branch. And, for the most part, most individuals going in, who are subject to very similar restrictions in the executive branch, choose to divest, including very successful millionaires and billionaires who——

Mr. DAVIS. Are there tax——

Ms. HEMPOWICZ [continuing]. Are in the Executive Branch.

Mr. DAVIS. [continuing]. Incentives for divesting as a member of the Executive Branch?

Ms. HEMPOWICZ. You can receive—in the same way that I think some of the legislation would include here, if Members are selling their stock and they would incur a penalty, they would be able to get a certificate of divestiture, which would put off the—it wouldn't give them a benefit and it wouldn't give them a tax penalty.

It would simply maintain their status quo until after their government service, and then they would have to pay whatever taxes they would have had to pay on those assets, whatever they did with them whenever. Which is the same thing they do in the executive branch, sir.

Mr. DAVIS. All right.

I know I am out of time, but Mr. Sherman did raise his hand.

Do you know the number of Members of Congress that would be able to afford that?

Mr. SHERMAN. I don't. As my colleague Ms. Hempowicz mentioned, divestment is an option, and it is an option that I think is preferable, from the standpoint of—certainly of CREW. QBTs may work for some Members, but there are other options that Members should avail themselves of if——

Mr. DAVIS. Forced divestment.

Mr. SHERMAN. [continuing]. You pass a ban.

Mr. DAVIS. Forced divestment is the option you are talking about, right?

Mr. SHERMAN. Well, you use "forced." I would say that being in public service is a choice. And——

Mr. DAVIS. It is a choice.

Mr. SHERMAN [continuing]. So—

Mr. DAVIS. And that is——

Mr. SHERMAN [continuing]. The choice to divest——

Mr. DAVIS [continuing]. What I am concerned about with many of the proposals that are out there, that the choice for those who are not independently wealthy is going to be limited compared to those who are wealthy and can afford a qualified blind trust.

Mr. SHERMAN. I certainly am aware that there are more limited choices for individuals with less net worth than those with more, and I think this is another example of that. I think divestment remains a viable option.

Mr. DAVIS. Thank you for giving me the——

The CHAIRPERSON. The gentleman yields back.

Mr. Aguilar is recognized for five minutes.

Mr. AGUILAR. Thank you, Madam Chairperson. And I appreciate you holding this hearing and the opportunity to hear from our witnesses.

Despite what the Ranking Member said, my belief—and I feel I speak for folks on our side here—is, this is about gathering more information. This is about ensuring that we need to hold ourselves to the highest ethical standards, to realize that we need to follow the letter and the spirit of the law, and to recognize that there might need to be some changes along the way, and that the idea of crafting good public policy means that we have to weigh options and weigh equities, and that individuals who run for this office have to make choices on what public service and public sacrifice means.

And so, I appreciate hearing the information and reading the testimony as well.

Ms. Nagy, there have been ongoing conversations about the scope of covered persons within stock trading and ownership. Should stock-trading reform efforts capture Members alone, or should they include dependent children and the covered—covered individuals, senior staff members? What is the importance of the scope being widened here?

Ms. NAGY. Sure. Thank you, Representative Aguilar.

So I think the importance of the scope being wider relates to my very first point, which is that, if the concern is a conflict-of-interest concern about the ownership of securities and if the concern is that a Member of Congress may be tempted into self-interested decision-making, then that self-interested decision-making is also going to relate to one's spouse and potentially to one's dependent children, who that lawmaker has control, often, of the assets.

And so, insider-trading issues and trading issues are serious ones, but conflict-of-interest ones are very serious as well. And that is the area where Congress and the rules that apply to Congress and the laws that apply to Congress are very, very different than what currently applies in the Executive Branch and the Judicial Branch.

Mr. AGUILAR. I appreciate that.

Ms. Hempowicz—and then I will go again to Ms. Nagy on this question—there has been debate over the ideal enforcement mechanism within the STOCK Act. Some potential bodies: SEC, Securities and Exchange Commission; Department of Justice Office of the Special Counsel.

What are some of the challenges facing these specific enforcement mechanisms?

Ms. HEMPOWICZ. Yes, I think when we are talking about enforcement mechanisms that will go through the executive branch, we are going to run into Speech and Debate issues.

Our preferred enforcement mechanism runs through Congress. It is the one that you—I am sorry, these bills all run together at this point. But it is the—I think it is the Ban Conflicted Stock Trading Act, and it is the one led in the Senate by Senator Ossoff. I think that one has the clearest enforcement mechanism.

I think the high-level principles to consider with an enforcement mechanism is that, you know, any penalties would be meaningful, that it would be easy and simple to apply, and that the public can have confidence that it is being applied evenly across the board. And so there must be some transparency there.

And so, I think those are the three high-level principles. But if you are asking what my preferred mechanism is, it is the one in the bill led by Senator Ossoff.

Mr. AGUILAR. Ms. Nagy.

Ms. NAGY. So, I think the enforcement mechanism could get more complicated when there are various options to divest or put in a blind trust. I think the administration of blind trusts would be—the administrative challenges would be immense.

If we look at the difficulties that Members have had in complying with the STOCK Act's 45-day reporting requirement, adding more disclosures, more forms, more supervision does not seem, to me, the way to remedy the current problem.

I think the enforcement mechanism, the simplest one, is to say that Members of Congress cannot own covered securities. Exempt certain types of securities, like widely held diversified mutual funds, Treasury bills, others. There might be some other exceptions, and I think drilling down to that.

The simpler the prohibition, the easier the enforcement.

Mr. AGUILAR. I appreciate it.

Mr. Sherman, you were the only one that mentioned—I am sorry; you may not be the only one. But you specifically mentioned Federal resources in oversight mechanisms. And can you talk with me briefly about, you know, how we bolster the enforcement bodies to improve our ability to tackle insider trading and other conflicts?

Mr. SHERMAN. Absolutely.

I think it is incumbent upon this Committee to speak to the enforcement bodies, whether that is the OCE or the House Ethics Committee or some of the Federal law enforcement agencies that were mentioned, to understand their capacity and how much resources they would need to implement these policies.

I agree with my colleagues, though. I think the simplest and the cheapest mechanism of enforcement is to implement an absolute ban on Members and their families owning and trading individual stocks and other securities.

Mr. AGUILAR. Thank you, Mr. Sherman.

I yield back, Madam Chairperson.

The CHAIRPERSON. The gentleman from Georgia is recognized for five minutes.

Mr. LOUDERMILK. Well, thank you, Madam Chairperson.

A very interesting hearing. I think this is something we should be discussing and talking about.

But one quick question. I learned Mr. Sherman was part of the Ethics Committee just since I have been here. I am curious, how many ethics violations were prosecuted per year?

I mean, I know that it is politicized and there are tons of ethics complaints for political purposes. But, on an average, how many years of Members of Congress where we held accountable for ethics violations?

Mr. SHERMAN. With apologies, I don't know the answer to that question. I served on the Ethics Committee before the STOCK Act was passed.

Mr. LOUDERMILK. Well, not just with stocks; with anything.

Mr. SHERMAN. Sure——

The CHAIRPERSON. Would the gentleman yield?

Mr. LOUDERMILK. Yes.

The CHAIRPERSON. Because I was chair——

Mr. LOUDERMILK. Okay.

The CHAIRPERSON [continuing]. Of the committee at that time. And we had a very vigorous enforcement mechanism at that time, one that Mr. Sherman was very actively——

Mr. LOUDERMILK. Right. What I was——

The CHAIRPERSON [continuing]. Involved in.

Mr. LOUDERMILK [continuing]. Wondering is just, whether it is stocks or not, how many ethics violations do we catch people with that are prosecutable or however you—the term you want to use—in a year?

Mr. SHERMAN. Again, I would be guessing if I——

Mr. LOUDERMILK. Okay. That is fine.

Mr. SHERMAN [continuing]. Gave you a hard answer——

Mr. LOUDERMILK. But there are some?

Mr. SHERMAN [continuing]. But there——

Mr. LOUDERMILK. Yeah.

Mr. SHERMAN [continuing]. Are some——

Mr. LOUDERMILK. Which is a violation of an existing rule or regulation or law, correct?

Mr. SHERMAN. Absolutely.

Mr. LOUDERMILK. Okay. That is all I was wondering.

I will turn it over to Ms. Schulp.

Insider trading. Has there been insider trading done by Members of Congress in the last few years?

Ms. SCHULP. There have been no prosecutions brought under the STOCK Act provisions on insider trading.

Mr. LOUDERMILK. So there were some——

Ms. SCHULP. But there have been Members of Congress convicted of insider trading.

Mr. LOUDERMILK. Right. Right. Which is illegal.

Ms. SCHULP. Correct.

Mr. LOUDERMILK. Okay.

I am kind of getting to a point, is that a misconception that we have here is that government can change behavior. It cannot. Laws can't change or shape behavior. It can only punish for violations of those.

If we enact something like this that restricts the rights and the freedoms of individuals—and everybody in this Committee is a free American citizen that has rights. And part of the rights, as explicitly defined by our Founders, was the right to participate in a free-market society. The first stock market came in 1790, shortly after the ratification of our Constitution. It is part of a free-market system. It is no different than having a bank savings account that you can draw interest.

Now, I am speaking from somebody—if you pulled the disclosures on me—and maybe you have—you found that there were none. No stock trades. Why? Because the minimal stock trades that I do is below the threshold of reporting. And so, it is not going to affect me, what you do, one way or the other.

Let me also bring this up. It is ironic—I am on the Financial Services Committee, and part of the oversight that we have is the stock markets, the SEC. There was an article that was written about me a few months ago or a year ago criticizing me that I have oversight and regulatory authority over the stock markets, and I don't even trade stock so how could I know anything about it.

Versus, one of the reasons I started trading a few stocks on my own, so I could learn the intricacies of what I am doing. That is not a conflict of interest. That is using the interest I should have to further my knowledge, to know what is right, what is wrong, how do we do this, how can we correct these things.

Look, we cannot change behavior. At the founding of our country, there were four Federal felonies. Today, we have rooms of code books, of laws, but murders still happen. If government could change behavior, we would have no murders, we would have no thefts, we would have no fraud. We can't change behavior. If we enact a law that prohibits Members of Congress from owning or trading stocks, it will still happen by bad players.

John Adams put it this way. He said, our Constitution is for a religious and moral people; it is wholly inadequate for the government of any other. What he was saying is, basically, the only way that you can control behavior is have such a strong and powerful government that it strips the freedoms away from everyone. If we have freedoms, if we have rights, you must accept that bad people are going to do bad things, but you put the guardrails in for punishment of those things.

So, I am just—whatever happens here, we have to keep in mind that every person in this room is an American citizen that has rights and freedoms, and part of that right and freedom is to participate in a free and fair market economy.

And, if you look, there are so many ethics controls on Members of Congress right now, I think you are going to run some people out.

And I just—I wanted to take my few minutes to bring a different perspective on this from somebody who it is not going to make a difference to me personally. But it does make a difference to me as an American citizen.

And, yes, seventy percent—look, if you polled a Republican district after it came out that the Speaker's husband made all these millions of dollars on a stock trade, I guarantee you most of them would say, yes, ban it. Ban it. But if you went to a Democrat area, it probably wouldn't be as much. Because people are emotional, and our Founders put in a system that was slow and methodical so we wouldn't react emotionally but thoughtful, based on law and protecting freedoms.

And so, Madam Chairperson, I see my time has expired, and so I yield back the time I no longer have.

The CHAIRPERSON. The gentleman yields back.

The gentlelady from Pennsylvania is recognized for five minutes.

Ms. SCANLON. Thank you so much. And thank you for having this hearing.

I mean, obviously, the public has been appalled by the reporting we have seen about Members of Congress and the Senate using inside information to profit themselves. The whole point of public service is to serve the public, not line politicians' pockets.

I do think there is a lot of usefulness in establishing firmer laws. I would have to disagree that laws have no impact. Thinking of smoking or speeding, we certainly set some guardrails. And when people know what the rules are, they follow them better.

I certainly find myself in the unusual position of agreeing with the Ranking Member that we do need to do a better job of educating Members of Congress about what those guardrails are. Because the whole process of getting here is such a firehose of information that this is not one that is well-emphasized.

A couple of you have talked about Executive-Branch guidelines being maybe something we should be considering. And maybe we could start with Mr. Sherman. I know, Ms. Nagy, you also discussed this. If anyone else wants to chime in.

Can you talk about how the Executive-Branch guidelines with respect to stock trading might inform what we are trying to do here and if there are any important differences we should be thinking about?

Mr. SHERMAN. Sure.

Well, the conflict-of-interest statute that applies to the Executive Branch but does not apply to Congress creates provisions that ban Federal employees from working on specific matters where they have a conflict with their financial holdings. It doesn't name specific securities. It is pretty broad. It applies to spouses, and it applies to dependent children.

I think that is a good model for Congress, in part because we know Congress thought that it was important. I don't know why Congress opted themselves out of it.

I think that is a good floor, with the recognition, however, that Members of Congress are differently situated than executive-branch employees, because Executive-Branch employees have the opportunity to recuse themselves from matters where there is a financial conflict.

Again, with respect to Members of Congress, it hurts your constituents if you are recused from any matter that is within the purview of Congress. It denies them representation. Which is why the prophylactic measures for Members of Congress should be higher, not lower, than applied to members of the executive branch.

Ms. SCANLON. Ms. Nagy.

Ms. NAGY. Yes. Thank you.

If one is a member of the Executive Branch and one is charged with shaping healthcare policy, one cannot own healthcare stocks, full and simple. Sometimes it is prohibited by statute directly. Sometimes it is prohibited because of the conflict-of-interest statute that Mr. Sherman just took us through.

Members of Congress can own stocks and shape healthcare policy. And they do.

Ms. SCANLON. Yes.

Ms. NAGY. And they are complying with all current rules and all current disclosure requirements when they do, which says to me a change needs to be made.

We have had instances where Legislative-Branch officials, where lawmakers, when the President nominates them to move to the Executive Branch, have to sell their stocks because they can't do their jobs. But they went for decades doing their jobs here in Congress, and they were complying with congressional rules, which says to me congressional rules need to change. I think a Federal statute is the way to change that.

Ms. SCANLON. Okay. And it is interesting since the scope is so broad. I mean, we have to deal with wars in Ukraine and we have to deal with childcare tax credits and everything in between. So that is an interesting distinction.

I think you had something, Ms. Hempowicz.

Ms. HEMPOWICZ. Yes. I just want to—in addition to what my colleagues have said, I think it is also important, the Executive Branch provides a really good model for any particular exemptions or unique situations as they come forward.

You know, I know people have asked questions about, how would you handle cryptocurrency underneath the new restrictions? I think the Executive Branch you know, has provided a really good roadmap of how to do that.

There are also questions about you know, non-nuclear families and how would they be approached. The Executive Branch has had restrictions that are stronger, in many ways, than what is being considered right now for Congress and has found a way to make it work—and has found a way to make it work without deterring successful people or, you know, people from the lower economic ring in our society from participating in the Executive Branch while under those stricter restrictions.

Ms. SCANLON. I have a gazillion more questions. Also wondering how much public financing of campaigns would help. But thank you, and I will yield back.

The CHAIRPERSON. A vote has been called on the Floor of the House. We have two votes. So, we will recess at this time to go vote. It is probably going to take at least forty minutes to come back, so you may want to go get a cup of coffee or something. We have at least three Members who have questions, and there has been discussion of maybe having a second round if you all are game to stick around for that.

So, at this point, we will recess, and we will come back promptly after the second vote.

[Recess.]

The CHAIRPERSON. We are waiting for Jennifer Schultz to rejoin. Apparently she is downstairs and on the way. We have the gentlelady from New Mexico, but she has not yet arrived, and Mr. Raskin is participating online. We don't know the answer, so I will turn to myself for some of the questions that I have.

Let me just say, Mr. Davis has talked about his gigantic stock portfolio, which he inherited as a child. I have never purchased or sold a stock or a share of stock. So in some ways, this is very much an educational experience for me on the nuances and the questions that are before us. I am sure the Ranking Member has had the same experience I have had, people asking questions, what about this, what about that, that, by and large, I don't have the answer to.

So let me pose this question. Several people have—I think the goal, if I am hearing everyone correctly, is that a Member of Congress should not be able to personally benefit financially from the information they receive because they are a Member of Congress, or because of decisions that they are making as a Member of Congress. I think most of us agree with that. So the question is how to address that. I think, as people have asked me questions, it seems like there are more complications than it would seem at first blush.

So let me ask the fundamental question which has been asked to me: Why stocks would be different than other assets? For example, we have Members of Congress who are allowed—who own a business that they owned before they were elected, an insurance company or a store or, you know, car dealership, whatever, and the decisions being made, or the information received could have an impact on the value of that asset.

We have Members of Congress who have professional licenses. When I chaired the Ethics Committee—Mr. Sherman may remember this—you are not allowed to practice your profession as a Member of Congress to avoid conflicts of interest. The medical doctors approached the Committee with the point that if they didn't practice a certain number of hours, they would lose their license, and they would never be able to practice medicine again. And so, we arranged for a scheme where the medical doctors could put in the number of hours that they needed to retain their license, and the remuneration could be no more than what was necessary to pay their malpractice insurance for doing those hours. And I think that has worked reasonably well.

On the other hand, you know, Medicare reimbursements, a whole variety of things impact what an M.D. will, in the future, be able to expect as an income stream. The same with dentists or even attorneys. You don't have the minimum hour issue with M.D.s, but if you vote on something that provides for a private right of action that is remunerative in the future, you could benefit from that.

So why are those issues different than stocks? Whoever could answer that would be helpful.

Ms. NAGY. Well, thank you. So stock in individual publicly traded companies is the low-hanging fruit, and let's go after the low-hanging fruit. It would be great to go up the tree and get higher-reached fruit, and as we do it is more nuanced and it is more complicated. But a total of hundreds of millions of dollars of assets of Members of Congress are currently invested in publicly traded company stock.

The CHAIRPERSON. I understand that, and I think there is a genuine desire to address the issue. But from a policy point of view, what is the distinction?

Ms. NAGY. So the policy distinction is if we rid that interest and shift it, because it is not completely abolished, basically then the stock is held in diversified investment funds. Members of Congress in a diversified fund would not have as much impact.

The CHAIRPERSON. Let me ask you this: Members of Congress—most American middle-class American families, the single most important financial asset they have is their personal dwelling. I think that is true—other than the extremely wealthy people in Congress, and there are some, that is true for most of us. Obviously, there are a lot of things that can impact real estate. I mean, mortgage rates and the like. Should we require Members to sell their homes?

Mr. SHERMAN. So, I think we have to recognize two things: One, there are conflicts of interest with respect to most of what Members of Congress do, right? Members set tax policy, and, presumably, they all pay taxes.

I think how we have to approach this is a balancing test that takes into consideration the risk of a conflict of interest materializing in a way that impacts Members in their representation of their constituents, as well as consideration of how large a pool of individuals the conflicts that Members have impacts beyond them, right? For example, with tax policy, or with owning a home, or paying for college, right?

These are things that affect the general public, you know, across income levels, across various different factors. And I think everyone agrees that it is reasonable to understand why Members of Congress, you know, are elected to make policy with respect to those issues without selling their homes or, you know, taking other extreme measures.

With respect to individual stocks and other assets that are under discussion with some of these proposals, one, they impact a much smaller class of assets than the public possesses in a much more substantial way. I don't think there is any way to compare the stock portfolio, or the financial portfolio, of the average American as compared to the portfolio of the Member of Congress.

The CHAIRPERSON. I agree with that. I am understanding your conflict rules. I think they match the conflict rules of the House, in terms of if it broadly impacts the public, you know, it doesn't—but let's talk about businesses.

Lawyers—and I know several lawyers who are in the House, and if they were in private practice, they had to shut their practice down and lay off all the employees. Other people who don't have management of businesses, they can keep those businesses.

Why would those businesses be treated differently than a stock portfolio, because, obviously, most Americans don't own a business? How would that be dealt with and what is the policy distinction, if any, being made?

Mr. SHERMAN. I don't think they necessarily should. I will give you an example from the depths of the Ethics Manual. With respect to recusal, there is a provision, an example in the Ethics Manual that says it is okay for Members of Congress who own a brewery to vote on prohibition legislation. That seems like an obvious conflict of interest that any normal person could understand that the congressional ethics rules not only explicitly allow but articulate as an example of how Congress should function.

I think that is a problem. I think there are lots of businesses and interests in privately held companies that present the same level of conflicts of interest that we are seeing with stock trades. As Professor Nagy said, I think we should handle as much as we can, as judiciously as we can, but that doesn't mean that other conflicts don't exist and shouldn't be addressed.

I think there is a reasonable test and a line that can be drawn. We have seen it with small farms and things like that, but certainly they present the same conflicts that we are dealing with here.

The CHAIRPERSON. Let me ask a question, and maybe this is a dumb question, but as I indicated earlier, I have never purchased any stock or sold any stock. If you look at my disclosures, however, it looks like there are all these stock trades, but what it is, my husband, he is a lawyer, he is a sole practitioner, and he has a retirement fund that some guy at the bank manages for him.

I don't know what he is doing, and I suppose my husband could find out, but I don't think he does. We just say, don't buy fossil fuels, don't buy tobacco, don't buy gambling, and sometimes he doesn't even adhere to that. But that is not a blind trust, but, in fact, we don't know what he is doing.

Could you substitute the very burdensome—and, you know, there are problems in terms of what you put into a blind trust, but the asset requirements and all the blind trust rigmarole with a more simple approach that you attest under penalty of perjury, the Member, that you don't know and you are not directing and you are not receiving information, and the person who is doing the investing does the same penalty-of-perjury attestment. Does that work?

Ms. HEMPOWICZ. If I could jump in on this one.

The CHAIRPERSON. Sure.

Ms. HEMPOWICZ. The scenario you describe, kind of where the holdings are in a retirement account, is not necessarily what we are talking about here. I think that would likely follow the current restrictions.

I think the benefit of a blind trust is that there is a statutory definition there. The individual is, like you are saying, under penalty of perjury, but in there, it is the individuals administering the trust also have a professional responsibility and will receive professional penalties.

But to the point that you are making, that you don't own individual stocks and Ranking Member Davis that you made also along those lines, that puts you in line with most of the American public. Again, I think the restrictions on how they would apply to Members of Congress would not shut Members of Congress out of the financial market, as was suggested earlier. It would simply limit their ability to engage in those markets with financial instruments that don't pose those same conflicts as individual stock ownerships do and then would allow—and I think also to your point earlier about what the goal is here, absolutely the goal is to make sure that Members of Congress aren't corruptly using information that they have.

I think the goal must be a little bit bigger than that too, and it has to be that Congress crafts ethics rules and laws that are strong enough that the public doesn't even have to worry about whether or not that is happening.

The CHAIRPERSON. It is the appearance as well.

Ms. HEMPOWICZ. The appearance of a conflict is as damaging to the integrity of the institution as an actual conflict.

The Chairperson. Let me ask a couple of questions that I have been asked. If the goal is basically to keep the Member of Congress in the dark—and if they don't know something they can't act upon it, I overstate that—it occurs to me that, to some extent, the STOCK Act reporting undercuts that whole goal. For example, once a year, my husband grumbles about it. He must fill out this form because I don't know what is going on. Once a year I find out what he has been doing. I guess there is that value as a spouse. But otherwise, I would never know. So, to some extent, the reporting aggravates the situation, and you must report for tax purposes and then once again, for disclosure purposes.

Would it make more sense to align the dates of the disclosure so that the tax and reporting are at the same time? You don't at least have two disclosures. That is something we could do by adjusting the disclosure time for Members to coincide with tax time. Would that help some?

Mr. SHERMAN. My understanding is that the reason why the FD date is a month out is so that Members can file their taxes without having that butt up against the deadline for FDs.

I think, frankly, taking a poll of Members and figuring out if the intent behind that accommodation makes sense would be a reasonable approach to figure out if it is just running in place.

The CHAIRPERSON. Let me ask a couple of questions that have been asked to me by various Members, and I won't go into any names, but people wonder about this.

A Member of Congress is estranged from a spouse, not divorced, but it is obviously heading that way. The non-Member spouse is engaging in rampant stock trading and will not comply with requests of the Member spouse.

I mean, should we have a provision where you could say, This is out of control, we are estranged? I mean, you are going to hold a Member accountable for something they can't control. What do we do with that?

Ms. HEMPOWICZ. Yeah. I think one thing to consider, or two things to consider with any exemption or potential exemption would be—well, one good roadmap is to look how the executive branch has handled it. Again, you know, they have had these similar restrictions for over sixty years.

I think kind of the bigger, broader principles for Congress to consider when thinking about this or any kind of exemption to this rule is that any exemption takes you further away from what the American people are asking for. And so, I think, as a threshold matter, Congress should ask itself could this exemption undermine public trust? And if the answer to that is yes, I think Congress should then ask, Is it absolutely necessary that we figure it out in this legislation, or is it something that we could do in regulation?

I also think if it has the potential to undermine public trust and is not absolutely necessary, I urge Congress to resist the urge to address every individual instance that may come up, because I think it just further complicates a system that really benefits from simplicity.

The CHAIRPERSON. That may be the answer that people have for the other specific questions I have been asked. People have asked about, is it 527, these education accounts? Is that the right code section? Would that be covered? Because Members contribute for their children and for their grandchildren so they can go to college. And people are worried that, you know, most of the Members of Congress could earn a lot more money in the private sector than they are earning here. We are not asking for a pay raise. We are just noting that if you can't support your kid's college, you know, endeavors, and you have to quit——

Ms. NAGY. So, I think you are referencing 529, a saving plan for tuition.

The CHAIRPERSON. Yes.

Ms. NAGY. And the way those usually work is that you put in your monthly contributions, or annual contributions, and it is typically directed into a diversified fund, sometimes an index fund, sometimes——

The CHAIRPERSON. So it is because you don't control it, it would not be covered.

Ms. NAGY. Correct. You do not control the individual stocks in the portfolio, in the basket of stocks that the fund would own.

The CHAIRPERSON. And that would be true for retirement funds as well, I would assume?

Ms. NAGY. Correct.

Ms. HEMPOWICZ. It is in addition to because you don't control them, but also, they meet definitions of being diversified. And so, you are not having—that you don't have that same impact on any one sector, or any one particular company as you would with individual stock ownership.

The CHAIRPERSON. Okay. Let me ask a question that has come up. You inherit stock. I will give you an example. We no longer have the stock, but my husband's Aunt Mary was married to an oil field worker, and it turned out that she had stocks in an oil company that Ed has received and he had died. And she never had kids, so her nieces and nephews inherited it, which we didn't want.

But what do you do when that happens, either for you or your minor children, you have acquired it, but not intentionally?

Mr. SHERMAN. Well, I would go back to what my colleague, Ms. Hempowicz, said. I think we are designing an ethics regime for the Legislative Branch. We should start from the principle that public service is a public trust and establish as stringent and clear a rule as possible. There are always going to be unique family situations as unique as the 535 Members of the House and the Senate, but we can't develop an ethics regime like that.

Certainly, the Ethics Committees, if they are given authority to enforce these rules, can come up with some reasonable regulations that account for very specific and likely to occur exceptions, but I think we need to start from a general rule——

The CHAIRPERSON. So we would leave that to we are going to have to check with the Ethics Committee on their capacity to do that. I mean, for example, one of the questions I have been asked is what if your spouse is employed in a company and their compensation is stock options. Do they have to work for free?

Mr. SHERMAN. I think most of the proposals under consideration right now would allow for the spouses to be compensated in the way that their employers decide.

I know you didn't ask this, but I will also just say explicitly, I think Members of Congress should get a raise. It is important for government ethics. It is important——

The CHAIRPERSON. Well, I appreciate that, but that is not going to happen. So——

Mr. SHERMAN. Fair enough.

The CHAIRPERSON [continuing]. I will just make that very clear.

You know, there are many, many other questions, but I have taken more time than really is fair. I thought about this a lot, and

I appreciate the testimony, because you all have a high level of expertise in this area.

I see the gentlelady from New Mexico has arrived, so we will turn to her for her questions.

Ms. LEGER FERNANDEZ. Thank you, Chairperson Lofgren. And this line of questioning really highlights the fact that it is not easy, right? It is an area where we are trying to deal with multiple Members of Congress who each have their own unique histories of why and how they came here.

I will say that over the last few months, one of the top reasons why my constituents have been reaching out to me is that they want to urge a ban on individual stock ownership for Members. So, it is not something that is in a vacuum. We are dealing with—our constituents are asking us to make sure that we have that separation, that we have that independence, and that our best interests in what we do financially is not at all tainted by what we do here.

You know, and I agree with that. I don't think Members should be in the business of owning or trading individual stocks. When I first got elected, soon after it was brought to my attention that my retirement portfolio had—my 401(k) had a very modest amount in an individual stock. So, I had to go in and actually take the extra effort to actually say, no, get rid of that. I do not want to have there be any question at all. As the Chairperson noted, I was not aware of that until it was brought to my attention, and I immediately asked them to turn it into something else. I don't know what you can do with it, just turn it into something else.

The other thing that strikes me is that we are talking about choice. I love the fact that that word came up a lot, because when we run, when we ask voters to elect us, which we have to do every two years, we are making a choice at that time. So, if we know that we have a large portfolio of stocks, and if it is known in advance that once you get elected, you are going to have to divest yourself of those stocks or put it in a blind trust if you have enough to make sure that you can pay the cost and deal with the complexity. That is a choice you are making. When you are asking—you are asking voters to trust you. So, we need to return that trust. As long as we know that is what we need to do, then that becomes part of the decision-making process.

But there is an issue of timing, and so, like how long would you recommend that a Member of Congress, once elected, be allowed before they must engage in that divestment? If they inherit something, what is reasonable then? I mean, because we want to be able to provide a period of reasonableness that everybody knows about.

And I will ask that of the panel. So, I see several of you shaking your heads up and down. So, what would you answer to that?

Ms. HEMPOWICZ. I will be faster than I usually am. You know, I think the important thing, again, to consider and look and see how things have been handled in the executive branch, and so, I think the timelines that are given there might be a good indicator.

I think also, you know, some people have suggested that maybe any additional restrictions shouldn't go into place until a Member wins reelection, and I think that may also be—that may also be reasonable.

You know, I think we are certainly not trying to create an ethics program that is impossible to comply with. We are trying to do the opposite. And it should be as simple to comply with as possible.

Ms. LEGER FERNANDEZ. Right. And waiting until reelection allows that Member to make the choice as to whether they will continue to ask for that.

Mr. Sherman.

Mr. SHERMAN. Agreed. I think the executive branch provides some examples. I also think that the time period should be with all deliberate speed, particularly relative to the two-year term of service that Members are elected to.

So I have seen some proposals which are ninety days, 120 days. That seems not unreasonable, but I think with all deliberate speed is advisable.

Ms. LEGER FERNANDEZ. And Professor Nagy, as you answer that, I have another one and since I don't have a lot of time I will just see if you want to answer that. And also, I mean, we keep pointing to the executive branch and its models.

Are there instances of something that is in the Executive Branch that doesn't quite fit within a congressional setting, and what are some of those examples?

Ms. NAGY. So, on the timing issue, I would say that I think a number of the bills actually, particularly for inheritance, raise 180 days as the time that someone would have to divest. I think the consideration there is that sometimes the stock market is not doing what one wants it to do, and that gives a little bit of time there.

I would also say for any divestment that is required under legislation that Congress enacts, I would also recommend the same type of rollover of capital gains tax that is currently in force, that Congress has currently put in the statute for the Executive Branch.

I think that if someone sells assets, sells stock and other securities because they are ordered to do so, and they move that into a diversified mutual fund, the law should be written so that capital gains is deferred.

Going to the Executive Branch, that is the rule in the Executive Branch. I think what the Executive Branch has, because in most instances in the agency, it is not an outright prohibition, although there are exceptions. The FCC is one exception. Don't own telecommunication stock. The disclosure forms that Executive Branch officials complete allows the ethics agency to determine whether there is a conflict of interest or is not. And then that then triggers the need for recusal or divestiture. And clearly, that is not the instance here. Mr. Sherman before referenced the sort of brewery example that is codified in the manuals there. The House and Senate Ethics Manual reference stock ownership, and explicitly say that divestment is not required even if Members own stock in companies that directly and substantially affect the legislation.

So, the problem is greater than the current law allows this. It is that the problem is that the current rules in the House and Senate safe harbor this.

Ms. LEGER FERNANDEZ. Thank you. My time is expired, Madam Chairperson.

The CHAIRPERSON. The gentlelady yields back. The Ranking Member is recognized for our second round.

Mr. DAVIS. Thank you, Madam Chairperson. Again, this is a great hearing. I do truly appreciate the witnesses.

Going back to our previous conversation, I just—I think what we are hearing from our witnesses is that Members have a choice. You can either go into a qualified blind trust that I have already established, I and most Members of Congress would never qualify for, for one company, LPL's minimum investment of $500,000. Don't have it. Most Members don't. Or divest. Divest individual stocks that then we will get accused of getting a special privilege of deferred capital gains.

So those types of—you must take into consideration what the perception is when you all come up with what you think might be a great idea for Congress, but we are in a different perception. CREW might call us corrupt if we take that tax break. Who knows?

I am focused on the middle-class Member, and I just don't believe that forcing middle class Members to divest an ownership portion of a family farm, or to divest ownership in a business that their spouse may be a part of, their dependent children, I just think it is untenable.

Would you all agree that your proposals are mainly geared toward the wealthiest Members of Congress?

Ms. HEMPOWICZ. I wouldn't. No, I wouldn't say so.

Mr. DAVIS. Okay. All right.

Ms. Nagy, you testified earlier you don't believe the ballot box is sufficient to be a check on Members of Congress, drawing analogies to different rules with different branches of government. I want to point out that only two people in the Executive Branch are elected, zero in the Judicial Branch. We have had no discussion on the Judicial Branch right now.

I don't think that analogy compares apples to apples. I mean, we are accountable to 800,000 people every two years. We have a job interview called an election.

Ms. NAGY. So, my testimony before was that the ballot box is not a sufficient remedy to ethics, because ethics affect the Nation, affect everybody. And so, if a Member has conflicted investments, and is generating a public perception that the reason he or she is advocating for legislation is to juice the value of their portfolio, that is a national problem. And the fact that a small——

Mr. DAVIS. That is a corruption problem. That is, again, those corrupt Members. But most——

Ms. NAGY. That is not corrupt. It is allowed. If I may just respond. It is not corruption. It is currently completely within—the House and Senate rules do not prohibit a Member from owning stock or owning an investment and advocating for the direct benefit of that investment unless—and there is an unless—unless they are the sole beneficiary of that legislation.

Mr. DAVIS. Do you have a number that your research has put forth that would determine how many Members of Congress are doing that?

Ms. NAGY. How many are doing it? How many people are advocating for legislation because it benefits their own portfolio?

Mr. DAVIS. Yes.

Ms. NAGY. I am not sure how that can be quantified.

Mr. DAVIS. I agree.

Mr. SHERMAN. If I may.

Mr. DAVIS. Hold tight. I appreciate it, I would be glad to get to you. I have a limited amount of time. I don't control the Committee. But this is a great time to be able to ask a lot of different questions.

So, as we look ahead—all right, let's look back. We were coming into a pandemic, right? We, in a bipartisan way, virtually unanimously created the Paycheck Protection Program. It benefited a lot of small businesses that are attached to stocks, maybe Members own.

Should every Member of Congress, because they may have voted for that program, was that a corrupt thing because we tried to save the economy? Is that something that you can go back and say Members of Congress benefited?

I mean, in my particular case, I was accused, because my family Members got PPP loans, of trying to benefit my own family when I have no financial interest. But that is settled in the election.

I mean, I think you can try to find a connection to everything we do, but again, most Members of Congress I truly believe, Republicans and Democrats, want to do the right thing. I don't trade stocks because I don't want to have to fall into some gray area of a reporting issue, but I think there is an issue that we don't start with what we have. We follow transparency rules. We file ethics disclosures that most people in the American public don't.

So, with that in mind, one last question. And I know, Mr. Sherman, you have probably more experience with this than most. Knowing the ethics disclosures that all of us file, and they are easily available, did any of you go research mine while we were on break? Darn it. I was hoping you would. You could get it easily.

And then we have the STOCK Act transaction paperwork that I have never used, but others have. So, I don't know anything about that. But I file my own ethics disclosure because I want to go talk to the Ethics Committee staff to make sure I am doing everything right.

But is there anything in our current disclosure requirements that is lacking, that you would say needs to be more transparent and, if so, what is it?

Mr. SHERMAN. Yes. So, I appreciate the question. One, I would note that the only way to really know if a Member is acting on a financial conflict of interest is to see their communications about that policy, but Congress is exempt from the FOIA, right?

So, when you talk about true transparency, I think there is some transparency, but the transparency with respect to Members of Congress, how laws are made and their financial conflicts of interest pales in comparison to the executive branch.

I would also note that with respect to financial disclosures and periodic transaction reports, they are accessible to I think the folks on this side——

Mr. DAVIS. What are they missing?

Mr. SHERMAN. I think they are not easily accessible to the public. They are not machine readable. You can only view one document at a time. So, if, for example, one of your constituents wanted to review all of your transactions over the course of your tenure——

Mr. DAVIS. And so you have an accessibility——

Mr. SHERMAN [continuing]. They cannot easily do that.

Mr. DAVIS. You have an accessibility based on something that can be fixed. Make it more searchable and sortable on the Clerk of the House website. But I am talking about the disclosure itself.

Mr. SHERMAN. Sure. Disclosure does not correct conflict.

Mr. DAVIS. The disclosure itself is our ability, as Members of Congress, it is our ability to tell our voters and tell every person in America here is our financial picture for our entire household. Here it is.

Chairperson Lofgren, you know, she laid out how her personal situation is. Each time that ethics disclosure comes, I know what mine is because I do it, but what on that disclosure, what are we not doing that gives corrupt Members of Congress the ability to hide wealth, or hide trades, or hide something that you, as a former Ethics Committee attorney, you used to see these corrupt cases, right?

Mr. SHERMAN. Yes.

Mr. DAVIS. What is it that you would recommend we do to fix the current transparent process, because I think that is a key point that in a lot of recommendations, we start from where we are today rather than where we were before this transparency existed?

And we start at a point rather than looking back and saying, what can we correct to make the periodic transaction report better? What can we correct to make the ethics disclosure PFD better?

Mr. SHERMAN. I think, you know, as I said, making them more easily accessible to the public, machine readable. But also, we have had, as you mentioned, 59 Members of Congress violate the STOCK Act since 2019. So whatever enforcement mechanisms are in place clearly aren't working.

Maybe there is education——

Mr. DAVIS. Education.

Mr. SHERMAN [continuing]. As you mentioned, which I think is incredibly important, but the penalties aren't high enough to promote the compliance that I assume that Members want and that the public is demanding.

Mr. DAVIS. I am going to ask you guys one more time, and anybody else can answer this. This is my last question. I am sorry, Madam Chairperson.

The CHAIRPERSON. That is all right. I was going to ask if you would yield for a follow-up——

Mr. DAVIS. I will yield.

The CHAIRPERSON. [continuing]. On that, because we have had a lack of compliance. And one of the things I am thinking about, you know, it could be somebody trying to hide something or, more likely, somebody just messed up, and that the penalties—you know, it is the same amount of penalty whether it is $100 trade, or $1 billion trade, and maybe we ought to stagger/phase the penalties based on the dollar amount.

Mr. DAVIS. And that is something as we develop what would be a final piece of legislation to address these issues, I would love to work with you on that, Madam Chairperson.

But where we are right now, I mean, Congress today versus 25 years ago is much more transparent. I actually led a group when we were in the majority that made every MRA expense searchable and sortable. I mean, even the most liberal good government groups said nice things about me. I know it was tough, but they did. I know.

But there has got to be within the existing system—I mean, is there anything that we can do within the existing disclosure system that can be more transparent about what Members of Congress, what we do, because, I mean, we want to follow the rules.

And just immediately changing the rules, telling people you got to divest in your family farm, you have got to divest in your family business, you have got to divest in a stock that you may have inherited—and I will tell the chairperson I will gladly take ownership of any fossil fuel stock she inherits. I will hold that for you.

The CHAIRPERSON. My husband sold it.

Mr. DAVIS. I will take care of it for you.

But in the end, we want to do the right thing. We all try to do that right thing. What is it that we have in place today that can be better and could show what is happening in our financial picture that may not be shown today?

Ms. HEMPOWICZ. Ranking Member Davis, to your question, the transparency requirements currently on Congress have been enormously helpful in highlighting to the public that Members of Congress own and trade individual stocks.

And that is the issue that the public keeps rising up about and wants to be—and wants their voice heard on. It is not that they care about missed filing deadlines, or that they are concerned that Members aren't aware of the current rules. It is that every step of the way when the public becomes aware of what those current rules are, they are outraged that Members of Congress are allowed to engage in this behavior.

And so, I think just focusing on additional disclosure requirements or the existing nonprohibitions in the STOCK Act would be a tragically missed opportunity to engage with the American people on something they care a lot about and have told Congress they would like to see you act on.

Mr. DAVIS. I would argue that both Republicans and Democrats here, we engage with the American people on a regular basis.

Ms. Nagy, did you have a response to that?

Ms. NAGY. I did. I will just echo my colleague's statement. Assuming timely reporting, the problem is not what is hidden. The problem is what is in the sunshine. And the sunshine is causing individual constituents to question not only their Member's decision-making, but the entire Congress, or at least the large group that doesn't already have their assets diversified into widely held funds.

Constituents are questioning and members of the public are questioning what was the motivation that prompted the push for this legislation. And that is in the sunshine. It is not hidden, it is in the sunshine, and that is troubling.

Mr. DAVIS. Ms. Schulp, did you have any comment on that?

Ms. SCHULP. Yes, I have two comments to that. And one we keep coming back to the question of diversified funds. And I think it is an interesting, good question that we keep coming back to, but keep in mind that some of the questionable trading that happened during the COVID pandemic was in diversified funds. So the problems that we are discussing, and the conflicts that exist, are not nonexistent in diversified funds as well. It doesn't magically take care of the question of a conflict.

On the question that you pose directly with respect to what could be better in the disclosure now, I think the long lag between the time that trades happen and that periodic transaction reports are required to be filed is something to take a look at. And where I have had interactions with the public, I have heard calls for more timely and quicker disclosure on that front.

Corporate insiders are required to disclose within two days. That two is not a completely comparable situation to Congress, but having 30 or 45 days after a trade takes place is an exceptionally long period of time after that trade takes place for disclosure to happen.

Mr. DAVIS. I will end by this—and, again, thank you for giving me so much extra time. I do believe this discussion is extremely important. I look forward to working with each of you individually as we move forward.

But I will tell you, and I certainly hope this hearing allows my constituents more of an opportunity to think about this process. And I can tell you it is—I travel a lot when I am home. I haven't had a lot of constituents bring this up. I hope they do, because I want to explain to them the processes we have in place and get their opinions and their ideas.

I certainly hope those of you who have already put proposals together for divestment and qualified blind trust that we cannot afford, that most Members cannot afford to participate in, I hope you are willing to listen to how we can make the process better, and do it in a way that doesn't just encourage the ultra-wealthy to be the only ones to run for Congress.

So with that, I yield back.

The CHAIRPERSON. The gentleman yields back. Mr. Aguilar, you are recognized for five minutes.

Mr. AGUILAR. Thank you, Madam Chairperson. And I am happy to continue down the path and the conversation specific to kind of education and compliance. Mr. Straus, we have been talking about the, you know, PTRs, the periodic transaction reports, and the thirty days of covered financial transactions.

What remedial measures does the Ethics Committee have in place in the event that a Member or a staffer files a PTR incorrectly.

Mr. STRAUS. So thank you for the question. And my colleague, Mr. Sherman, may know more specifics on the details of some of this stuff, but, in general, when a filing happens, whether it is a PTR or a financial disclosure report, and there is an error on the form, which I am led to believe is not uncommon, right—they are complicated forms to fill out—the committee reviews the forms, notifies the filer, and the filer has time to correct that filing.

Most errors that occur on financial disclosure forms are de minimus errors. Things are put on the wrong line, you know, just mistakes that happen. And once that filing is identified as being wrong, an amendment can be filed.

The Ethics Committee is very clear that filing an amendment in and of itself does not have anything to do with potential wrongdoing, that most of the time—and a Member or a staff member can file an amendment on their own, too, if they realize that they have made an error, without prompting.

It is only after the potential that, you know, an error can be fixed, if someone chooses not to comply, that is when the committee might get involved in working with that person, either directly or indirectly, to figure out what is going on and whether a potential recourse might be necessary or not.

Mr. AGUILAR. Mr. Sherman.

Mr. SHERMAN. I think every staffer on the Ethics Committee remembers getting that one call from a Member about a question about the form that they submitted. Mr. Straus is exactly right. You know, Members file their FDs and PTRs, and there is a process to work with them to make sure that the information is accurate, and if there are questions they are asked, there is an opportunity to amend.

I think even on the investigative side, particularly with financial disclosures, you know, I think there is a presumption that we need to make sure that this form was filled out accurately and correctly. There is sort of a lean towards presuming that Members sometimes make honest mistakes, which we all do.

Mr. Aguilar. Mr. Straus, with respect to the remediation process, how does that differ within the Executive Branch?

Mr. STRAUS. So a Designated Agency Ethics Officer in the Executive Branch has prescribed tools that are potentially available to them, depending on individual circumstances. So when a filer puts a financial disclosure form into their DAEO, their Designated Agency Ethics Officer, and it is reviewed, the ethics officer is going to work with that individual on a case-by-case basis to choose the best remedy available, which could be divestiture. It could be recusal, as we have talked about. It could be the creation of a blind trust. But it also could be a voluntary transfer, right, to another job within an agency, depending upon what the circumstances is.

And so, those agency DAEOs have a lot of flexibility to work with that individual to come up with a solution that works for a particular case, depending on their financial situation, based on what is in the disclosure.

Mr. AGUILAR. I appreciate it.

Mr. Straus, CRS is known for their education, for helping us at every step of the way. The Ranking Member talked about opportunities for new Members to receive information.

What would you envision? What does a training session, you know, on this look like? You know, how should we think about scaling up the Member educational pieces of this process? No matter what road we pick, what should that look like?

Mr. STRAUS. Well, first I would say that I don't nor CRS presumes that education is not already occurring, and that there are requirements for that educational process to take place.

In the executive branch, the Office of Government Ethics works very closely with the Designated Agency Ethics Officers in each agency to train them so that they can then train the staff within each agency.

So ultimately, the Ethics Committee is the one responsible for holding those ethics trainings and for deciding the type of educational content, right, that might be included within that process, both for Members and for staff. I have never taken the training, certainly not the Member training on that particular topic, but to Mr. Davis' point earlier, more education is almost always preferable in these types of situations.

And probably the advice I give offices that call more often than anything else is, when in doubt in this space, ask for permission, don't ask for forgiveness. Call the Ethics Committee's advice and education staff and ask them rather than presuming to know what the answer is, even if you have gone through that training, just to make sure you are on the compliance side of whatever the circumstance might be.

Mr. AGUILAR. My situation is similar to the Ranking Member's in that, I handle this document, because it is about, you know, me, and it is about my circumstance and my household. I want to make sure that I do this right. But that often means I am reaching out to the committee directly and filing this as well.

I do think that there is a lot of space on the education side. The policy piece is why we are here, and it is something that we have to do, but I know that the chair, you know, feels strongly about giving Members the tools to do this job successfully, and I think that there is some space to do some more on the Member side.

Thank you. I yield back.

The CHAIRPERSON. The gentleman yields back.

We have had another vote called on the Floor. So I will just make a couple of comments. I think—I don't remember which witness expressed concern, but I know it has been expressed among certain Members that we not hold up whatever we are going to do relative to the Legislative Branch for changes in the Judicial Branch or the Executive Branch.

I don't think we should hold this up for that. On the other hand, I don't think we should hold up reforms in those areas too. So the obvious answer is not to put them all in one bill, but to let the processes move forward. And I think there is very strong evidence that we need additional measures in the Judicial Branch. I don't think it should be combined in one bill with this, but I don't think we should hold it up while we are working on this.

A real simple question, and, you know, the ranges on disclosure, I have never understood that. It is like, okay, between zero and 10,000. Well, if it is five bucks, it means one thing, and if it is 10,000, it means something else. And you really can't tell what is going on. And then for people who are very wealthy, it is over $50,000. Well, maybe it is $1 billion. That would be something we would like to know.

What is wrong with just doing the actual dollar amount in the disclosure? Is there a reason for this?

Mr. SHERMAN. I think sometimes it is hard to be accurate, and Members definitely don't want to be inaccurate. But I agree with you. I think the demarcations could probably use a little bit of work.

The CHAIRPERSON. Okay. I am going to close out and just say that, without objection, the following items will be included in the record of today's hearing: The February 17, 2022, CRS report; a letter sent on March 28 to House leadership and this Committee from 19 Good Government organizations; an April 7, 2022, letter to this committee from the National Taxpayers Union; an April 7, 2022, letter to me from Representatives Krishnamoorthi, Ocasio-Cortez, and Neguse; and a March 17, 2022, Wall Street Journal article, "Dozens of Federal Judges Had Conflicts: What You Need to Know"; a December 10, 2007, Kansas Law Review article by Professor Megan J. Ballard, "The Shortsightedness of Blind Trusts."

The CHAIRPERSON. I would note, and we have had a lot of discussion about education for Members. As you know, this Committee is tasked with having a new Member orientation, which we take very seriously. We had significant training and information sessions on this and many other things over a two-week period.

Among other things, we had the Ethics Committee come in and discuss all their obligations and a discussion of the disclosure forms and the PTR reports and the like. However, as our only freshman on the committee said, it is like a firehose at a freshman orientation. So, the Ranking Member and I have been gossiping that maybe we should do a separate webinar or something of that nature on this, similar to what we have done with the Congressional Accountability Act that every Member has to do once a Congress or something of that nature. We can on work on that without legislation, obviously.

I will note that we very much appreciate our witnesses' time. I know it has been a little disjointed because of floor votes. We will ask if you would remain open to additional questions that we may send to you. The hearing record will be open for your responses.

And I don't know—Mr. Davis, we have got a vote on the floor. Anything you want to add before we adjourn?

Mr. DAVIS. Thank you very much. I certainly do look forward to sitting down with each of you individually and talking about how we can make the processes better.

The CHAIRPERSON. Thank you very much. Again, appreciation for the witnesses and, without objection, the Committee on House Administration is adjourned.

[Whereupon, at 12:29 p.m., the Committee was adjourned.]

QUESTIONS FOR THE RECORD

Congressional Research Service
Informing the legislative debate since 1914

MEMORANDUM May 31, 2022

To:	Honorable Zoe Lofgren
From:	Jacob R. Straus, Specialist on the Congress
Subject:	**Responses to Questions for the Record from April 7, 2022, Hearing of the House Administration Committee, "Examining Stock Trading Reforms for Congress"**

This memorandum provides answers to Questions for the Record received from the Committee on House Administration following an April 7, 2022, hearing titled "Examining Stock Trading Reforms for Congress."

Information in this memorandum is drawn from publicly available sources and may be of general interest to Congress. As such, all or part of this information may be provided by the Congressional Research Service (CRS) in memoranda or reports for general distribution for Congress.

1. A number of legislative proposals for financial conflicts of interest reform would effectively require hundreds of Members to establish new qualified blind trusts (QBT) all at the same time. The law requires that new trusts be approved by an official's supervising ethics office, which includes reviewing the trust agreement, verifying the independence of the proposed trustee, and confirming that certain assets may be placed in a QBT. Do you think the congressional ethics committees currently have adequate capacity and resources to administer approvals for a significant number of new qualified blind trusts? Please expand.

Should Congress adopt a proposal that would create the potential for additional qualified blind trusts (QBTs) or amend existing financial disclosure or periodic transaction reporting requirements, it could result in the required review of additional documents by the supervising ethics offices of the House (Committee on Ethics) and the Senate (Select Committee on Ethics). Congress may face decisions on whether such additional review might present administrative challenges.

Whether or not the supervising ethics offices currently have the resources necessary for the review of additional filings, including approving new QBTs, could not be fully analyzed by CRS using the limited public information it was able to identify. CRS has not located any public comments or statements from either the House Ethics Committee or Senate Select Ethics Committee on the need for additional staff or resources. Without a public record comment from the committees, CRS cannot determine whether the House Ethics Committee or the Senate Select Committee on Ethics currently has adequate resources to carry out the potential for additional administrative ethics functions.[1] For the 117th Congress, the House Ethics Committee received approximately $7 million for expenses.[2] In the 116th Congress (2019-2020), the House Ethics Committee reported that it employed between 24 and 29 professional, non-partisan staff.[3] According to the *Report of the Secretary of the Senate*, in FY2021, the latest year available, the Senate Select Committee on Ethics spent approximately $3 million, and employed approximately 17 staff.[4] The adequacy of resources would also likely depend on the timeline for implementation of any new requirements, the number of Members, officers, and congressional staff impacted, and the length of time required to review and certify each filing.

2. As you testified, the various legislative proposals offered to date differ with respect to whether they would amend the Ethics in Government Act (EIGA), amend the STOCK Act, amend both, or create new law. What are the ramifications of these different approaches to this issue? In particular, what consequences do these choices have for the authority of supervising ethics offices and for enforcement by those or any other government entities?

In the 117th Congress (2021-2022), the legislative proposals introduced and discussed at the April 7, 2022, hearing would amend the Ethics in Government Act, and/or the STOCK Act, both, create new law, or amend the House Standing Rules.[5] The potential legislative path of any proposal likely depends on the goals of individual Members, the committees of jurisdiction, and the relevant House or Senate rules and procedures.

Proposals to amend the Ethics in Government Act and/or the STOCK Act, or to create new law all generally focus on codifying new prohibitions on covered individuals from holding, purchasing, or selling covered assets or requirements for the disclosure of certain types of transactions. As lawmaking vehicles, bills to amend existing law or create new law would require the steps needed for enactment (that is,

---

[1] 5 U.S.C. Appendix §§101-112; P.L. 112-105. For a list of proposed bills to amend the Ethics in Government Act, the STOCK Act, or both in the 117th Congress, see testimony of Jacob Straus, Specialist on the Congress, Congressional Research Service, at U.S. Congress, Committee on House Administration, *Examining Stock Trading Reforms in Congress*, April 7, 2022, at https://cha.house.gov/committee-activity/hearings/examining-stock-trading-reforms-congress.

[2] H.Res. 1035 (117th Congress), agreed to April 28, 2022. U.S. Congress, House Committee on House Administration, *Adjusting the Amount Provided for the Expenses of Certain Committees of the House of Representatives in the One Hundred Seventeenth Congress*, report to accompany H.Res. 1035, 117th Cong., 2nd sess., April 21, 2022, H.Rept. 117-291 (Washington: GPO, 2022), p. 2. Expenses of the Senate Select Committee on Ethics are paid from the contingent fund of the Senate. See U.S. Congress, Senate, Committee on Rules and Administration, *Senate Manual: Containing the Standing Rules, Orders, Laws, and Resolutions Affecting the Business of the United States Senate*, 116th Cong., 2nd sess., S.Doc. 116-1 (Washington: GPO, 2020), §77, p. 123.

[3] Pursuant to House Ethics Committee Rule 6, all "staff [are] to be assembled and retained as a professional, nonpartisan staff." U.S. Congress, House, Committee on Ethics, *Rules*, 117th Cong., 1st sess., February 25, 2021, p. 11, at https://ethics.house.gov/sites/ethics.house.gov/files/documents/20210225%20Committee%20Rules%20for%20the%20117th%20Congress%20%28FINAL%29.pdf#page=14. U.S. Congress, House, Committee on Ethics, *Summary of Activities One Hundred Sixteenth Congress*, 116th Cong., 2nd sess., H.Rept. 116-703 (Washington, GPO, 2020), p. 8, at https://www.govinfo.gov/content/pkg/CRPT-116hrpt703/pdf/CRPT-116hrpt703.pdf#page=13.

[4] U.S. Congress, Senate, Secretary of the Senate, *Report of the Secretary of the Senate from April 1, 2021 to September 30, 2021*, 117th Cong., 1st sess. S.Doc. 117-8 (Washington: GPO, 2021), p. B-2-56, at https://www.govinfo.gov/content/pkg/GPO-CDOC-117sdoc8/pdf/GPO-CDOC-117sdoc8.pdf#page=2110. In the Executive Branch, the Office of Government Ethics (OGE) reported that 42% of agencies need additional resources to manage their ethics program, with human capital and technology needs most requested. Office of Government Ethics, CY2020 questionnaire #9, p. 5, at https://www.oge.gov/web/OGE.nsf/0/BF327B2CC50A959D8525870C00663796/$FILE/AQ%20Summary%20Report%20January%202022%20correction.pdf.

[5] U.S. Congress, House Committee on House Administration, *Examining Stock Trading Reform for Congress*, 117th Cong., 2nd sess., April 7, 2022, at https://cha.house.gov/committee-activity/hearings/examining-stock-trading-reforms-congress.

House and Senate passage, as well as a successful override process should the President veto the bill). Consequently, any future changes would generally require additional lawmaking.[6]

Some of the proposals introduced in the 117th Congress include provisions that would apply to Members for a period *after* they depart the House.[7] Depending on the legislative vehicle, these proposed restrictions might have varying effects. Using a lawmaking vehicle (e.g., a House or Senate bill or joint resolution) could have the effect of creating new law that might be parallel to existing "revolving door" provisions that restrict covered former government officials from engaging in certain activities for a period of time after they leave government service.[8]

Some proposals would amend the House Standing Rules (rather than amending the Ethics in Government Act or creating a new law) to place additional restrictions on Members of Congress.[9] In that case, changes to House Rules could be interpreted as having a somewhat more limited scope. Any changes would apply only to current Members of the House while they remain in office. House Rules do not apply to Members once they leave office and do not apply to Senators.[10] The duration may also be more uncertain, since House Rules are considered and adopted at the beginning of each Congress, and changes to the rules package may be proposed.[11]

The decision to amend existing law or create new law would not necessarily have an impact on enforcement by the supervising ethics office. For details on enforcement provisions of various legislative proposals in the 117th Congress, see the discussion of "Penalties for Non-Compliance" in my written testimony.[12]

---

[6] Amendments to these laws, or establishment of others, would be subject to the regular rules of the House and Senate. (For example, such legislative vehicles would not be privileged for consideration or disposition in the Senate; therefore, the support of three-fifths of the Senate may be necessary to reach final passage in that chamber). For more information, see CRS Report 98-425, *Invoking Cloture in the Senate*, by Christopher M. Davis; and CRS Report 96-548, *The Legislative Process on the Senate Floor: An Introduction*, by Valerie Heitshusen.

[7] H.R. 336 (117th Congress) and S. 3494 (117th Congress).

[8] For more information on the revolving door, see 18 U.S.C. §208 and CRS Report R45946, *Executive Branch Service and the "Revolving Door" in Cabinet Departments: Background and Issues for Congress*, by Jacob R. Straus.

[9] Resolutions to amend House rules are privileged for floor consideration if reported by the House Committee on Rules.

[10] See also, *INS v. Chadha* (45 U.S. 919 (1983)), holding that the actions of one chamber cannot alter the legal rights of those outside the legislative branch. Traditionally, when a Representative or Senator departs the House or Senate, the House Ethics Committee or the Senate Select Committee on Ethics loses jurisdiction over the former Member. For example, the House Committee on Ethics notes "As a general matter, the Committee's investigative jurisdiction extends to current House Members, officers and employees. When a Member, officer, or employee, who is the subject of a Committee investigation, resigns, the Committee loses jurisdiction over the individual." House Ethics Committee, *Summary of Activities*, 116th Congress, p. 14; and House Rule XI, clause 3(a)(2).

[11] For more information on adopting the Rules of the House, see CRS Report RL30725, *The First Day of a New Congress: A Guide to Proceedings on the House Floor*, by Christopher M. Davis.

[12] Testimony of Jacob R. Straus, Specialist on the Congress, Congressional Research Service, at U.S. Congress, House Committee on House Administration, *Examining Stock Trading Reforms For Congress*, 117th Cong., 2nd sess., April 7, 2022, at http://docs.house.gov/meetings/HA/HA00/20220407/114485/HHRG-117-HA00-Wstate-StrausJ-20220407.pdf.

3. You testified that in the executive branch, Designated Agency Ethics Officers have a range of options or remedies or tools to propose addressing a covered official's financial conflict of interest, including recusal, creation of a qualified blind trust, divestiture, and others. Does the Office of Government Ethics provide statistical information about the usage of these tools? For example, is data available about how many covered officials used each of those tools in a particular year? What appeals or waiver options are available to an official in the executive branch for whom a DAEO recommends divestment of a particular holding?

The Office of Government Ethics (OGE) does not provide statistical information on the frequency of various remedies used by Designated Agency Ethics Officials (DAEOs).[13] Once a covered employee files a public or confidential financial disclosure report with the agency, the DAEO reviews the filing to ensure its completeness and to identify holdings or liabilities that might violate or appear to violate federal law, executive orders, or agency-specific statues or regulations.[14] The DAEO must complete the review within 60 days.

Following the review, the DAEO is to certify the filing. If the DAEO does not believe they have enough information to certify the filing or if the filing is incomplete, they can ask the filer for additional information. For certain individuals, (e.g., the DAEO, nominees and appointments requiring presidential appointment and Senate confirmation, and employees of the Executive Office of the President) filings are forwarded by the agency to OGE for final certification.

If upon review the DAEO determines a conflict of interest exists, they can, if necessary, negotiate with the filer to remedy the conflict. There are several remediation options,[15] including disqualification (recusal), divestiture, resignation or reassignment, waiver, or the establishment of a qualified blind or diversified trust.[16] Remediation efforts are case-specific, with the DAEO generally instructed to consider the employee's circumstances and position in the identification and remediation of potential conflicts of interest.[17]

Waivers to certain conflicts of interest provisions are available by law, regulation, or executive order.[18] For example, the Ethics in Government Act provides for the availability of waivers for reporting requirements under certain circumstances. The law states:

> §101. Persons required to file
>
> (i) The supervising ethics office for each branch may grant a publicly available request for a waiver of any reporting requirement under this section for an individual who is expected to perform or has performed the duties of his office or position less than one hundred and thirty days in a calendar year, but only if the supervising ethics office determines that-

[13] 5 C.F.R. §2638.104(c).

[14] 5 C.F.R. §2634.605.

[15] 5 C.F.R. §2634.605(b)(6).

[16] 5 C.F.R. §2634.802(a)

[17] 5 C.F.R. §2634.605. For more information, see CRS In Focus IF11904, *Financial Disclosure: Identifying and Remediating Conflicts of Interest in the Executive Branch*, by Jacob R. Straus; and CRS In Focus IF12019, *Executive Branch Ethics and Financial Disclosure Administration: The Role of Designated Agency Ethics Officials (DAEOs)*, by Jacob R. Straus.

[18] Waivers are available under Executive Order 13989, "Ethics Commitments by Executive Branch Personnel," 86 *Federal Register* 14, January 25, 2021, at https://www.govinfo.gov/content/pkg/FR-2021-01-25/pdf/2021-01762.pdf; 18 U.S.C. §208(b)(1); 5 C.F.R. §2635.502(d); and 5 C.F.R. §2635.503(c).

(1) such individual is not a full-time employee of the Government,

(2) such individual is able to provide services specially needed by the Government,

(3) it is unlikely that the individual's outside employment or financial interests will create a conflict of interest, and

(4) public financial disclosure by such individual is not necessary in the circumstances.[19]

In June 2017, OGE issued a report on the issuance of certain waivers and authorizations from executive branch agencies, including the Executive Office of the President (EOP), for executive branch appointees between May 1, 2016 and April 30, 2017.[20] OGE reported that a total of 60 waivers were issued in the covered time period.[21] In recent years, agencies have reported additional waivers to ethics pledge requirements and to 18 U.S.C. §208(b)(1) and §208(b)(3).[22] **Table 1** reports the number of waivers issued from 2017 through 2020.

Table 1. Number of Waivers Issued by Agencies Pursuant to 18 U.S.C. §208(b)(1), 18 U.S.C. §208(b)(3), and Executive Order 13770, 2017-2020

Year	18 U.S.C. §208(b)(1) and 18 U.S.C. §208(b)(3) Waivers	E.O. 13770 Waivers
2017	340	37
2018	117	15
2019	459	22
2020	409	3

Sources: CRS Review of OGE questions for CY2016-CY2020. Office of Government Ethics, *CY17 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, June 5, 2018, revised August 29, 2018, pp. 3, 32, at https://www.oge.gov/web/oge.nsf/0/87394876D4CD3D708525865300703F1E/$FILE/2017%20AQ%20summary%20FINAL%20(rev.8.10.18).pdf; *Results from the 2018 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, Revised August 5, 2019, pp. 7, 19, at https://www.oge.gov/web/oge.nsf/0/5C524EAA4E38E9B48525865300703F25/$FILE/2018%20AQ%20summary%20doc%20FINAL%207.11.19%20(minor%20typo%20corrected%2012.5.19).pdf; *Results from the 2019 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, pp. 6-7, at https://www.oge.gov/web/oge.nsf/0/44B8C7071 9A52E3A852586530070037C/$FILE/2019%20AQ%20Summary%20Report%20FINAL.pdf; and *Results from the Annual Agency Ethics Program Questionnaire, CY 2020: A Snapshot of the Executive Branch Ethics Program*, Updated August 31, 2021, pp. 9-11, 22, at https://www.oge.gov/web/OGE.nsf/0/BF327B2CC50A959D8525870C00663796/$FILE/AQ%20Summary%20Report%20January%202022%20correction.pdf.

[19] 5 U.S.C. Appendix §101(i).

[20] Office of Government Ethics, "Data Call for Certain Waivers and Authorizations," PA-17-02, April 18, 2017, at https://www.oge.gov/Web/OGE.nsf/0/0FBCBBA2F3949979852585BA005BEC45/$FILE/PA-17-02.pdf. The data call asked for waivers under five authorities, Executive Order (E.O.) 13770 (issued by President Trump), E.O. 13490 (issued by President Obama), 18 U.S.C. §208(b)(1), 5 C.F.R. §2635.502(d), and 5 C.F.R. §2635.503(c). Both President Trump's and President Obama's executive orders were subsequently repealed. E.O. 13770 was repealed by E.O. 13983 (86 *Federal Register* 6835) and E.O. 13490 was repealed by E.O. 13770 (82 *Federal Register* 9333).

[21] See CRS Insight IN10721, *Office of Government Ethics: Role in Collecting and Making Ethics Waivers Public*, by Jacob R. Straus; and Office of Government Ethics, "Certain Waivers and Authorizations Issued Between May 1, 2016-April 30, 2017," June 2, 2017, at https://oge.gov/Web/OGE.nsf/Resources/Certain+Waivers+and+Authorizations+issued+between+May+1,+2016+-+April+30,+2017.

[22] 18 U.S.C. §208 prohibits employees from participating in any particular government matter that has a direct and predictable effect on their personal financial interests. For more information, see 5 C.F.R. §2640.

Any remediation decision is generally a negotiation between the DAEO and the filer.[23] There is not a one-size-fits-all solution to conflicts of interest, as each individual filer's financial circumstances are different and the response is generally tailored to the individual's needs in relation to their position in the government.[24] For example, for presidential nominees, OGE advises that

> The process begins when the prospective official completes a financial disclosure report. Once filed, ethics officials in the agency where the filer intends to serve, the White House, and OGE work together to identify potential conflicts. These potential conflicts are addressed using an ethics agreement where appointees detail, in writing, the actions they will take to resolve the conflicts. Such actions may include selling certain financial holdings and resigning from outside positions. Unless otherwise specified in the ethics agreement, appointees agree to take the specified actions within 90 days of confirmation by the Senate.[25]

Ethics agreements are between the employing agency and the employee. Any appeal or waiver provision would be included in existing law or regulations. For example, 18 U.S.C. §208 "does not provide for an appeal or review of the employing agency's decision," in identifying a conflict of interest and coming to a remediation agreement with the employee.[26]

4. Under current law and practice, what regular reporting – if any – is made about overall compliance by filers in each branch, as well as penalties or late fees assessed and other enforcement activity? Do supervising ethics offices or any other enforcement authorities – such as the Department of Justice or the Securities and Exchange Commission – provide any public accounting in this regard?

Compliance

OGE reports that at least 99% of public filers and 98% of confidential filers have filed reports when required under the Ethics in Government Act. **Table 2** reports the number of public and confidential filers between calendar year 2016 and 2020, the most recent report available, and the percentage of required filers who filed their statements with their designated agency ethics office.

Table 2. Office of Government Ethics Reporting of Public and Confidential Financial Disclosure Filers, CY 2016-2020

	Total Public Filers			Total Confidential Filers		
Calendar Year	Required	Filed (%)	Percent	Required	Filed (%)	Percent
2016	25,680	25,479	99.0%	352,216	369,446	105.0%
2017	28,501	28,237	99.0%	357,032	355,334	99.5%

[23] Office of Government Ethics, "Responsibilities of the Designated Agency Ethics Official (DAEO)," *Resources for Ethics Officials*, at https://www.oge.gov/Web/OGE.nsf/ethicsofficials_conflict-resolution.

[24] Office of Government Ethics, "Analyzing Potential Conflicts of Interest," at https://www.oge.gov/Web/OGE.nsf/a716ba6e5e826838852585ae005546c0/f029088beda3de04852585b6005a1e0e?OpenDocument.

[25] Office of Government Ethics, "Ethics Agreements: Where Ethics Obligations Become Action," July 24, 2019, prepared by Dale Christopher, Deputy Director for Compliance, at https://www.oge.gov/Web/OGE.nsf/Leadership%20Notes/29C259912C91CCEC852585B6005A22BF?opendocument.

[26] Office of Government Ethics, "Letter to an Employee dated March 12, 1992," 92x10, March 12, 1992, at https://www.oge.gov/web/oge.nsf/0/2F65F14F58BB23D2852585BA005BEEB5/$FILE/6715ac41f43649cbb87164444b2cbae42.pdf.

Calendar Year	Total Public Filers			Total Confidential Filers		
	Required	Filed (%)	Percent	Required	Filed (%)	Percent
2018	26,094	25,935	99.0%	354,714	353,300	99.6%
2019	27,133	27,012	99.6%	370,361	362,719	98.0%
2020	26,824	26,742	99.6%	368,654	365,069	99.0%

Sources: CRS Review of OGE questions for CY2016-2020. Office of Government Ethics, *CY16 Annual Agency Ethics Program Questionnaire Results: A Summary of the Executive Branch Ethics Program*, July 7, 2017, updated June 2018, pp. 17, 21; *CY17 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, June 5, 2018, revised August 29, 2018, pp. 25, 30; *Results from the 2018 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, Revised August 5, 2019, pp. 23, 25; *Results from the 2019 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, pp. 22, 26; and *Results from the Annual Agency Ethics Program Questionnaire, CY 2020: A Snapshot of the Executive Branch Ethics Program*, Updated August 31, 2021, pp. 25, 29.

Notes: Percentages calculated by OGE.

Neither the House Ethics Committee nor the Senate Select Committee on Ethics report on compliance by required House or Senate financial disclosure filers.[27]

Late Fees

OGE further reports data on public filers who were granted extensions, granted waivers of late filing fees, and who paid late filing feels. **Table 3** reports those numbers between 2016 and 2020, the most recent year available.

Table 3. OGE Reported Public Financial Disclosure and Periodic Transaction Report Filings and Late Fees, 2016-2020

Year	Granted Filing Extension		Granted Waiver of Late Filing Fee		Paid Late Filing Fee	
	Financial Disclosure	Periodic Transaction Report	Financial Disclosure	Periodic Transaction Report	Financial Disclosure	Periodic Transaction Report
2016	4,660	213	268	350	87	90
2017	3,802	317	170	440	67	77
2018	4,319	328	240	409	73	94
2019	4,525	400	253	429	46	126
2020	5,245	374	321	401	40	100

Sources: CRS Review of OGE questions for CY2016-CY2020. Office of Government Ethics, *CY16 Annual Agency Ethics Program Questionnaire Results: A Summary of the Executive Branch Ethics Program*, July 7, 2017, updated June 2018, p. 18; *CY17 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, June 5, 2018, revised August 29, 2018, pp. 26-27; *Results from the 2018 Annual Agency Ethics Program Questionnaire: A Snapshot of the Executive Branch Ethics Program*, Revised August 5, 2019, p. 24; *Results from the 2019 Annual Agency Ethics Program Questionnaire: A Snapshot of*

[27] U.S. Congress, House Committee on Ethics, *Summary of Activities One Hundred Sixteenth Congress*, 116th Cong., 2nd sess., December 31, 2020, H.Rept. 116-703 (Washington: GPO, 2020), pp. 7, 11-13, at https://www.govinfo.gov/content/pkg/CRPT-116hrpt703/pdf/CRPT-116hrpt703.pdf; and U.S. Congress, Senate, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 116th Congress, Second Session," 116th Cong., 2nd sess., January 28, 2020, at https://www.ethics.senate.gov/public/_cache/files/0392be1b-d9c9-430a-85bd-872f59fec372/annual-report---cy2019---published-1-28-2020.pdf.

the Executive Branch Ethics Program, p. 25; and *Results from the Annual Agency Ethics Program Questionnaire, CY 2020: A Snapshot of the Executive Branch Ethics Program*, Updated August 31, 2021, p. 28.

Notes: Financial disclosure is filed using OGE Form 278e; see Office of Government Ethics, "Executive Branch Personnel Public Financial Disclosure Report (OGE Form 278e)," at https://www.oge.gov/web/OGE.nsf/OGE%20Forms/FE904FADB163B45A852585B6005A23E8/$FILE/OGE%20Form%20278e%20(Nov%202021%20508%20PDF%20version).pdf?open. Periodic transaction reports are filed using OGE Form 278-T; see Office of Government Ethics, "Executive Branch Personnel Public Financial Disclosure Report: Periodic Transaction Report (OGE Form 278-T)," at https://www.oge.gov/web/OGE.nsf/OGE%20Forms/78E3B27A68F437DC852585B6005A23E9/$FILE/OGE%20Form%20278-T%20Nov%202019_accessible.pdf?open.

Neither the House Ethics Committee nor the Senate Select Committee on Ethics report data on late fees.[28]

Prosecutions

OGE provides a yearly accounting of conflict of interest prosecution. Each year, OGE conducts a survey of prosecutions involving the conflict of interest criminal statutes (18 U.S.C. §§202-209) and other related laws. OGE notes that "the survey highlights how the Department of Justice enforces the criminal conflict of interest laws, and is a useful resource ethics officials can use to educate employees about how these laws apply in real-world situations."[29] OGE maintains webpages that contain data from the survey organized by the number of prosecutions involving each law organized by year and by statute.[30] **Table 4** provides the total number of cases and statute from 1990 to 2020, the most recently available data.

Table 4. Office of Government Ethics "Conflict of Interest Prosecution Surveys Index" Compiled Results, 1990-2020

Statute	Number of Cases
18 U.S.C. §201 - Bribery of Public Officials and Witnesses[b]	21
18 U.S.C. §203 - Compensation for Matters Affecting the Government[c]	16
18 U.S.C. §205 - Claims Against and Other Matters Affecting the Government	7
18 U.S.C. §207 - Post-Employment Restrictions[d]	40
18 U.S.C. §208 - Official Actions Affecting Personal Financial Interests	151
18 U.S.C. §209 - Dual Compensation for Official Duties	65
5 U.S.C. app. 4 §101 - Persons Required to File Under EIGA	1
5 U.S.C. app. 4 §104 - Failure to File or Filing a False Public Financial Disclosure Report Under EIGA	5
18 U.S.C. §2 - Aiding and Abetting an Offense Against the United States	1
18 U.S.C. §371 - Conspiracy to Commit an Offense Against the United States or to Defraud the United States	12

[28] U.S. Congress, House Committee on Ethics, *Summary of Activities One Hundred Sixteenth Congress*, 116th Cong., 2nd sess., December 31, 2020, H.Rept. 116-703 (Washington: GPO, 2020), pp. 7, 11-13, at https://www.govinfo.gov/content/pkg/CRPT-116hrpt703/pdf/CRPT-116hrpt703.pdf; and U.S. Congress, Senate, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 116th Congress, Second Session," 116th Cong., 2nd sess., January 28, 2020, at https://www.ethics.senate.gov/public/_cache/files/0392be1b-d9c9-430a-85bd-872f59fec372/annual-report---cy2019---published-1-28-2020.pdf.

[29] Office of Government Ethics, "2020 Conflict of Interest Prosecution Survey," LA-21-08, August 2, 2021, p. 1, at https://www.oge.gov/Web/OGE.nsf/0/1B505A4C17E7289685258726004F63B7/$FILE/LA-21-08.pdf

[30] Office of Government Ethics, "Conflict of Interest Prosecution Surveys Index (by Statute)," at https://www.oge.gov/Web/OGE.nsf/Resources/Conflict+of+Interest+Prosecution+Surveys+Index+(by+Statute). See also, Office of Government Ethics, "Conflict of Interest Prosecution Surveys (by Year)," at https://www.oge.gov/web/oge.nsf/Resources/Conflict+of+Interest+Prosecution+Surveys%20(by%20Year).

Statute	Number of Cases
18 U.S.C. §1001 - Making False Statements or Writings/Committing Acts of Concealment[e]	48
18 U.S.C. §1018 - Making and Delivering a False Certificate or Writing	8
18 U.S.C. §1343 - Wire Fraud	12
18 U.S.C. §1346 - Honest Services Fraud	12
18 U.S.C. §1505 - Obstruction of Proceedings Before Departments, Agencies, and Committees	4

Source: CRS compilation of OGE data from Office of Government Ethics, "Conflict of Interest Prosecution Surveys Index (by Statute)," at https://www.oge.gov/Web/OGE.nsf/Resources/Conflict+of+Interest+Prosecution+Surveys+Index+(by+Statute).

Notes: Cases are not mutually exclusive. OGE counts some cases under multiple statutes.

a. OGE data for President George H.W. Bush's administration only includes data from 1990-1992.
b. Cases under 18 U.S.C. §201, include cases under sections 201, 201(b)(1), 201(b)(2), and 201(c)(1).
c. Cases under 18 U.S.C. §203, include cases under sections 203, 203(a)(1), and 203(a)(2).
d. Cases under 18 U.S.C. §207, include cases under sections 207(a)(1), 207(a)(2), 207(c), and 207(e)(2). For more information on post-employment restrictions, see CRS Report R45946, *Executive Branch Service and the "Revolving Door" in Cabinet Departments: Background and Issues for Congress*, by Jacob R. Straus.
e. Cases under 18 U.S.C. §1001, includes cases under sections 1001, 1001(a)(1), and 1001(a)(2).

Neither the House Ethics Committee nor the Senate Select Committee on Ethics report specific data on prosecutions.[31] In the House, should a Member be investigated for the potential violation of a law found in **Table 3**, it would be included in the case summary in the House Ethics Committee's annual *Summary of Activities*.[32] The Senate does not report similar data or case summaries.

5. You testified that, "Most errors that occur on financial disclosure forms are de minimus errors," and that once an error is identified, a filer can submit an amendment. Do the supervising ethics offices in each branch provide public information about amendments in the financial disclosure process, e.g., the number requested each year, the number filed each year, etc.?

From time to time, financial disclosure reports need to be amended. When an amendment is needed, it is filed with the individual's supervising ethics office. OGE notes in its financial disclosure guidance that amendments can be initiated by the filer or the reviewer. OGE states that "in some cases, a filer may initiate an amendment to a report. In other cases, a reviewer may make the amendment directly, either based on additional information from the filer or independent knowledge (e.g., indicating that a publicly traded mutual fund qualifies as an excepted investment fund)."[33] Further, the House Committee on

[31] U.S. Congress, House Committee on Ethics, *Summary of Activities One Hundred Sixteenth Congress*, 116th Cong., 2nd sess., December 31, 2020, H.Rept. 116-703 (Washington: GPO, 2020), pp. 7, 11-13, at https://www.govinfo.gov/content/pkg/CRPT-116hrpt703/pdf/CRPT-116hrpt703.pdf; and U.S. Congress, Senate, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 116th Congress, Second Session," 116th Cong., 2nd sess., January 28, 2020, at https://www.ethics.senate.gov/public/_cache/files/0392be1b-d9c9-430a-85bd-872f59fec372/annual-report---cy2019---published-1-28-2020.pdf.

[32] For example, see U.S. Congress, House, Committee on Ethics, "Historical Summary of Conduct Cases in the House of Representatives, 1798-2004," at https://ethics.house.gov/sites/ethics.house.gov/files/Historical_Chart_Final_Version%20in%20Word_0.pdf.

[33] Office of Government Ethics, "4.05: Report Amendments and Annotations," *Public Financial Disclosure Guide*, December 2018, p. 268, at https://www.oge.gov/web/oge.nsf/0/11E9ABAF6E128FF1852585B6005A2030/$FILE/Public%20Fin%20Disc%20Guide_Jan20

Standards of Official Conduct (now the House Ethics Committee) states that "in essence, the amendment, per se, should be submitted only as a result of the need to either clarify an earlier filing or to disclose information not known (or inadvertently omitted) at the time the original FD was submitted."[34]

Data on the number of amendments filed is not publicly available, to CRS's knowledge. Data on the number of financial disclosure filers is available for the executive and legislative branches. In the executive branch, OGE compiles the number of public and confidential financial disclosure filers (see **Table 2** under Question 4, above).[35] This data does not include the number of amendments filed.[36]

In the legislative branch, the House Ethics Committee and the Senate Select Committee on Ethics each report on the number of financial disclosure and periodic transaction statements filed in their annual reports. **Table 5** reports the number of financial disclosure and periodic transaction reports filed by Members, officers, and employees of the House and Senate in the 115th Congress (2017-2018), and the 116th Congress (2019-2020), the most recent data available.[37]

Table 5. Financial Disclosure and Periodic Transaction Reports Filed with the House Ethics Committee and the Senate Select Committee on Ethics

	House		
Year	Financial Disclosure	Periodic Transaction Reports	Senate[a]
115th Congress			
2017	3,092	2,106	4,141
2018	2,878	2,205	4,680
116th Congress			
2019	3,347	1,851	3,586
2020	2,984	1,871	3,712

Sources: House of Representatives: U.S. Congress, House, Committee on Ethics, *Summary of Activities One Hundred Fifteenth Congress,* 115th Cong., 2nd sess., H.Rept. 115-1125 (Washington, GPO, 2019), p. 8, at https://www.govinfo.gov/content/pkg/CRPT-115hrpt1125/pdf/CRPT-115hrpt1125.pdf#page=13; and U.S. Congress, House, Committee on Ethics, *Summary of Activities One Hundred Sixteenth Congress,* 116th Cong., 2nd sess., H.Rept. 116-703 (Washington, GPO, 2020), p. 8, at https://www.govinfo.gov/content/pkg/CRPT-116hrpt703/pdf/CRPT-116hrpt703.pdf#page=13. **Senate:** U.S. Congress, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 115th Congress, Second Session," January 29, 2018, at https://www.ethics.senate.gov/public/_cache/files/5d6fc616-d11f-4739-91de-6bf3bf82f5ed/annual-report-for-2017.pdf; U.S. Congress, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 116th Congress, First Session,"

19.pdf#page=268.

[34] U.S. Congress, House, Committee on Ethics, "Appendix D: Policy Regarding Amendments to Financial Disclosure Statements," *Instruction Guide: Financial Disclosure Statements and Periodic Transaction Reports, Calendar Year 2021*, p. D-1, at https://ethics.house.gov/sites/ethics.house.gov/files/documents/FINAL%202021%20FD%20Instructions.pdf#page=115.

[35] Office of Government Ethics, "Annual Questionnaire Summary Reports," *Oversight Summary Reports*, at https://www.oge.gov/web/oge.nsf/accessdocs_summary-reports. 5 C.F.R. §2638.207. Agency reporting of data to OGE satisfies the Ethics in Government Act requirement that agencies submit an annual report to OGE. 5 U.S.C. appendix §402(e)(1).

[36] For example, in CY2020, Question 35 states: "Report the number of public financial disclosure reports (OGE Form 278e) required to be filed by December 31, 2020, excluding SGEs, and the number of reports actually filed (i.e., received) by December 31, 2020; and in CY2020, Question 41 states: "Report the number of confidential financial disclosure reports required to be filed by December 31, 2020, excluding SGEs, and the number of reports actually filed by December 31, 2020."

[37] The Senate has reported data for 2021, the first session of the 117th Congress. It received 3,876 public financial disclosure and periodic disclosure of financial transaction reports in 2021. U.S. Congress, Senate, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics 117th Congress, First Session," January 29, 2021, at https://www.ethics.senate.gov/public/_cache/files/691e5e65-5b73-4e95-8cdb-de056570cb34/annual-report-for-2020.pdf.

January 29, 2018, at https://www.ethics.senate.gov/public/_cache/files/176dbba6-c624-4a8e-b77c-0e607238c6bc/annual-report-for-2018.pdf; U.S. Congress, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 116th Congress, Second Session," January 28, 2020, at https://www.ethics.senate.gov/public/_cache/files/0392be1b-d9c9-430a-85bd-872f59fec372/annual-report---cy2019---published-1-28-2020.pdf; and U.S. Congress, Select Committee on Ethics, "Annual Report of the Select Committee on Ethics, 117th Congress, First Session," January 29, 2021, at https://www.ethics.senate.gov/public/_cache/files/691e5e65-5b73-4e95-8cdb-de056570cb34/annual-report-for-2020.pdf.

Notes:

a. Senate numbers include financial disclosure statements and periodic transaction reports.

CRS was not able to determine if the judicial branch collects similar data. For more information on financial disclosure regulations in the Judiciary, see https://www.uscourts.gov/rules-policies/judiciary-policies/ethics-policies/financial-disclosure-report-regulations.

6. Is an "informal" blind trust where a third party manages the investment portfolio of the Member, and both the Member and the trust manager attest under penalty of perjury that no information on trades will be exchanged, a viable alternative?

As noted in my written testimony, qualified blind trusts are specific instruments that may be used to remediate real or perceived financial conflicts of interest.[38] Created in the Ethics in Government Act, qualified blind trusts

> confer on an independent trustee and any other designated fiduciary the sole responsibility to administer the trust and to manage trust assets without participation by, or the knowledge of, any interested party or any representative of an interested party. This responsibility includes the duty to decide when and to what extent the original assets of the trust are to be sold or disposed of, and in what investments the proceeds of sale are to be reinvested.[39]

The establishment of a qualified blind trust requires permission from a covered official's supervising ethics office (e.g., the House Committee on Ethics or the Senate Select Committee on Ethics for Representatives and Senators, respectively). Should a qualified blind trust be established to remediate a financial conflict of interest, the covered official "gives up the management of the assets to an independent trustee, who makes investment decisions for the individual's benefit without the individual's knowledge."[40] Further, the trustee must

> be an independent financial institution, lawyer, certified public accountant, broker, or investment advisor; there may be no restrictions on the disposal of the trust assets; [and] the trust instrument must limit communications between the trustee and interested parties.[41]

The use of qualified blind trusts can serve as a way to "immunize" a public official "from potential conflicts of interest stemming from assets held in the trust because the legislator-beneficiary would have no knowledge of the impact of official actions on [their] personal financial interests."[42] If a covered official places their assets in a qualified blind trust they are separated from the day-to-day decision making about their holdings, which can serve to remedy potential conflicts that might arise from decision-making that could impact their individual holdings.

---

[38] 5 C.F.R. §2634.401.

[39] 5 C.F.R. §2634.401(a).

[40] U.S. Congress, Senate Select Committee on Ethics, *Qualified Blind Trusts*, 114th Cong., 1st sess., September 2015, p. 1, at https://www.ethics.senate.gov/public/_cache/files/286a4cf9-5aab-40ef-9a6c-bf2278e79e38/qualified-blind-trusts-guide---october-2020.pdf.

[41] U.S. Congress, House Committee on Ethics, "Trusts," *Specific Disclosure Requirements*, at https://ethics.house.gov/financial-dislosure/specific-disclosure-requirements.

[42] National Conference of State Legislators, "Blind Trusts," at https://www.ncsl.org/research/ethics/blind-trusts.aspx.

Conversely, those that argue against the use of blind trusts say that the "early use of blind trusts may have originated from a desire to give the public appearance that a policymaker was avoiding conflicts of interest without actually blinding the policymaker to an asset that stood to influence the execution of official duties. Legislation establishing qualified blind trust rules has not solved this problem."[43]

Whether or not an "informal" blind trust might be a viable option depends upon the definition of an "informal" blind trust. CRS attempted to determine a definition of "informal" blind trust, but was unable to find a legal or practical definition of the term. In at least one instance, a scholar believed that the term "informal" blind trusts were used to collectively discuss the use of all blind trusts before "the Ethics in Government Act's standardization of the elements and operations of blind trusts...."[44] Even if a definition were available, CRS does not make recommendations about particular policy options.

[43] Megan J. Ballard, "The Shortsightedness of Blind Trusts," *University of Kansas Law Review*, vol. 56 (October 2007), p. 53.

[44] Ballard, "The Shortsightedness of Blind Trusts," p. 53.

Questions for the Record in response to
Testimony of Liz Hempowicz, Policy Director
Project On Government Oversight
Before the U.S. House of Representatives Committee on House Administration
On "Examining Stock Trading Reforms for Congress"
March 16, 2022

QFR 1. Why, in your view, is it important to include financial activity or transactions of covered officials' spouses and dependent children within the scope of any new restrictions on stock trading and ownership?

Response to QFR 1:

Covering the financial interests of spouses and minor children is necessary to resolve concerns about the appearance of insider trading. The public has no way to know if a Member of Congress discusses nonpublic information at home and should not have to wonder whether that information is influencing trades. Covering the financial interests of the Member's household would eliminate the appearance of insider trading by eliminating the opportunity for it. We need not debate whether Members are sharing nonpublic information that spouses are misusing; what matters is that the public reasonably perceives a risk of misuse.

The idea of covering the financial interests of an official's immediate family is not novel: Congress has done exactly that in the executive branch. The primary federal conflict of interest law, 18 U.S.C. § 208, has applied to the holdings of spouses and minor children of executive branch employees for 60 years. It is also instructive to remember that Congress currently requires Members to file periodic transaction reports regarding sales and purchases of the assets of their spouses and dependent children under both the Ethics in Government Act and the STOCK Act. This disclosure requirement further underscores the fact that Congress knows the finances of a member's household are inextricably linked.

Covering spouses and children is also necessary to address conflicts of interest in Congress. The financial interests of a Member's spouse or child have every bit as much potential to create a conflict of interest as a Member's own financial interests do. Again, Congress has shown it knows this to be true through its passage of conflict of interest laws for the executive branch. 18 U.S.C. § 208 requires executive branch employees to recuse from particular matters affecting the financial interests of their spouses and minor children, and regulations of the Office of Government Ethics at 5 C.F.R. § 2635.403(b) authorize an agency ethics official to order the divestiture of a conflicting financial interest in lieu of permitting recusal. Another example is the divestiture requirement applicable to members of the Federal Reserve's Board of Governors, 12 U.S.C. § 244, which the Board's interpretive regulations, at 5 C.F.R. § 6802.103, make clear applies not only to the members but also to their spouses and minor children. The same is true of the statutory divestiture requirement applicable to employees of the Office of the Comptroller of the Currency, under 12 U.S.C. § 11, which also applies to their spouses and minor children, as the interpretive regulations make clear at 5 C.F.R. § 3101.108. Another divestiture requirement is established for employees of the Office of Surface Mining Reclamation and Enforcement in 30 U.S.C. §1211, and interpretive regulations at 30 C.F.R. § 706.3 make clear that this requirement also applies to their spouses and minor children. The same is true for employees of the Bureau of Land Management under 43 U.S.C. § 11, according to interpretive regulations at 43 C.F.R. § 20.401.

Even when Congress has not directly extended divestiture requirements to the spouses and children of executive branch employees, federal agencies have such requirements in numerous regulations. For example, each of the following regulations expressly requires divestiture of specified assets by the spouses and children of covered executive branch employees:

5 C.F.R. § 3101.108;
5 C.F.R. 3201.103;
5 C.F.R. § 3401.102;
5 C.F.R. § 3501.104;
5 C.F.R. § 4101.103;
5 C.F.R. § 5501.104;
5 C.F.R. § 5601.102;
5 C.F.R. § 5801.102;
5 C.F.R. § 6001.104;
5 C.F.R. § 6401.102;
5 C.F.R. § 6801.103;
5 C.F.R. § 8301.103;
5 C.F.R. § 8301.107;
5 C.F.R. § 8401.102;
5 C.F.R. § 9001.104;
5 C.F.R. § 9401.106; and
17 C.F.R. § 140.735-2a.

As this long list of regulations reflects, there is a strong public interest in eliminating the conflicts of interest that arise from the investments of the spouses and children of federal officials.

QFR 2. Most of the introduced bills vary regarding what investments should be covered in a prohibition on trading and ownership and what should be exempted. Do you have specific policy recommendations for what specific types of covered investments should be included in any stock trading or ownership prohibition and what types of investments should be exempted?

Response to QFR 2:

POGO's recommended approach is that Congress should codify a ban on the ownership of any stock, bond, commodity, future, or other form of security, including an interest in a hedge fund, a derivative, option, or other complex investment vehicle as defined by § 2 of the Bipartisan Ban on Congressional Stock Ownership Act of 2022, H.R. 6678 and S. 3631.

Because Members have raised the desire for an option that would allow them to retain certain financial assets while addressing the specific concern about insider trading, we would not object at this time to Congress codifying the option for members to either divest ownership or place additional covered investments, as defined by § 2 of the TRUST in Congress Act (H.R. 336) and the Ban Congressional Stock Trading Act (S. 3494), in qualified blind trusts.

QFR 3. Should the following types of financial interests be subject to restrictions on ownership and/or trading activity? Why or why not?
a. Cryptocurrency
b. Initial coin offerings (ICOs)
c. Special purpose acquisition company (SPAC)
d. Real estate investment trust (REIT)
e. Options/futures
f. Commodities
g. Privately or closely held companies
h. Bonds

Response to QFR 3:

There is no principled rational or technical necessity for exempting these investments from restrictions imposed on other types of investments. They all pose potential conflicts of interests for Members of Congress and can be covered by the restrictions under consideration. Any exception for these investments would be based entirely on the unwillingness of Members of Congress to put the interests of the public they serve before their own personal interests.

Some in Congress have suggested that requiring the divestiture of small businesses would impose an emotional burden on Members who have grown attached to their investments. But no government ethics restriction will ever force an individual to divest a small business, for, after all, serving in Congress is a choice and not an immutable personal characteristic. Any Members of Congress who care more about their personal business endeavors than they care about the American people they serve would always have the option of returning to private life and continuing those business endeavors. Balanced against the emotions of these members is a strong public interest in preventing insider trading and eliminating conflicts of interest. The risk of insider trading may, in fact, be greater with small businesses than with large businesses, and the size of a business has no bearing whatsoever on the potential for conflicts of interest to arise.

QFR 4. How should a reform proposal address holdings that covered officials may have in a privately held company that subsequently goes public?

Response to QFR 4:

The STOCK Act, codified at 15 U.S.C. § 78u–1(i), already prohibits Members from participating in initial public offerings. The House Ethics Committee has issued the following guidance to Members:

> Section 12 of the STOCK Act amended the Securities Exchange Act of 1934 to ban Members, officers, and employees who file FD [Financial Disclosure] statements from participating in an Initial Public Offering (IPO) in a manner "other than is available to members of the public generally." The Committee notes that opportunities for the general

public to participate in an IPO are very limited. If you would like to participate in an IPO, we strongly recommend contacting the Committee in advance. As a result of the ban, filers will be required to indicate whether they purchased any shares that were allocated as part of an IPO on their FD Statement by checking the appropriate box. If you answer "yes" to the question because you received an IPO allocation, please contact Committee staff to discuss the disclosure format.[1]

QFR 5. The range and complexity of modern financial instruments and holdings posed challenges for the supervising ethics offices related to interpreting and enforcing the STOCK Act. In addition, new products and investment forms are constantly emerging, such as cryptocurrency and SPACs. What latitude should supervising ethics offices have to interpret the scope of covered investments, to grant extensions of time to comply with any new ownership and/or trading restrictions, or to consider and grant waivers?

Response to QFR 5:

The claim that some types of investments are too complex to address is simply not true. The U.S. Office of Government Ethics has shown that it knows how to address novel investment vehicles as they arise, and the ethics committees for the House of Representatives and the Senate could avail themselves of that agency's expertise by requesting assistance as needed. (For example, OGE issued a legal advisory (LA-18-06) on June 18, 2018, providing guidance on cryptocurrency.)

The failure to enforce the STOCK Act does not stem from the complexity of investments, it stems from a lack of political will to enforce the law. The complexity of an investment has no effect on the deadline for disclosing the sale or purchase of that investment. Moreover, prohibiting the ownership of these types of investments obviates the need for the ethics committees to address them. Take for example the questions that arose as to whether an investment in a SPAC constitutes participation in an IPO. That question arises only if Congress decides to allow members to invest in SPACs. A member who has not invested in a SPAC will not have to wonder whether investing in a SPAC is participation in an IPO. The concern about complexity this question addresses is one that arises if Congress persists in its failure to prohibit such investments.

For the same reason, authorizing waivers is a bad idea. The ethics committees do not have a strong track record for enforcement, and their members and staff are subject to political pressure. Therefore, they should not be permitted to grant waivers. A decision to grant the ethics committees the power to authorize exceptions would in all likelihood be tantamount to creating an across-the-board exception for all investments, inasmuch as the committees are unlikely to deny any request for a waiver.

QFR 6. Some observers have focused on shortcomings with the existing statutory requirements for and features of qualified blind trusts (QBTs). For example, as Mr. Sherman noted in his testimony, a filer knows what assets they put in a QBT at the time they

---

[1] U.S. House of Representatives Committee on Ethics, "Instruction Guide: Financial Disclosure Statements And Periodic Transaction Reports, Calendar Year 2018," at 12, 2018, https://ethics.house.gov/sites/ethics.house.gov/files/CY%202018%20Instruction%20Guide%20for%20Financial%20Disclosure%20Statements%20and%20PTRs.pdf.

create it, and current law requires the trustee to inform the covered official / trustor when an original trust asset is sold. He testified that, "qualified blind trusts could be a useful option if the Member is required to effectuate the sale of all of the assets that would go into that trust beforehand."

a. Would a requirement that the independent trustee dispose of any original trust assets within a certain period of time provide a meaningful improvement that could render QBTs a more effective and credible option than under current law? If so, do you have views about what deadlines for requiring sale of original trust assets might be reasonable? Should the tax implications of this proposal be addressed in anyway?

Response to QFR 6a:

Requiring the trustee of a qualified blind trust to divest the initial property of the trust would indeed ensure that the trust's beneficiaries are unaware of the trust's holdings. But making the trustee responsible for the divestiture is less than ideal because it is not the most transparent approach to divestiture. The law does not require either the trustee or the Member who is a beneficiary of the trust to file a periodic transaction report upon completion of the divestiture. As a result, the public has no way to monitor compliance with any divestiture requirement.

There are three other disadvantages to making the trustee, rather than the Member, responsible for divestiture:

(i) *Cost:* Paying a trustee to carry out the divestiture is an unnecessary expense that can be avoided by making the Member responsible for divestiture.

(ii) *Tax consequences:* If the Member wants to defer capital gains pursuant to a Certificate of Divestiture (assuming that these certificates become available to Members), the member will have to roll the proceeds of the sale into nonconflicting investments, such as diversified mutual funds. Any subsequent sale of the rollover property would trigger capital gains taxes. Therefore, neither the Member nor a trustee is likely to sell the rollover property – and, since the rollover property does not pose a conflict of interest, *there is no need to sell and no need for a blind trust*. This, in fact, is why there are no blind trusts in the executive branch. Rather than creating blind trusts, executive branch officials purchase diversified mutual funds and avoid the costs associated with blind trusts.

(iii) *Timeliness:* Making divestiture the responsibility of the trustee of a qualified blind trust adds a series of unnecessary steps prior to divestiture. These steps will inevitably delay a divestiture that could be accomplished immediately by a Member.

For these reasons, a better option would be to require the Members themselves, rather than trustees, to sell any prohibited property. Thereafter, any Members who still want to invest in qualified blind trusts should be required to put only cash in those trusts.

b. Are there other ways that the law could be changed to make QBTs a more effective option for deterring financial conflicts of interest?

Response to QFR 6b:

As currently structured, QBTs are not a silver bullet for managing conflicts of interest, but they do eliminate the potential for insider trading. As discussed in response to (a) above, the better option is to require a Member to divest conflicting financial interests.

If, however, Congress elects to require divestiture by the trustee (or not to require divestiture at all), POGO would recommend adopting a transparency provision that is contained in the Ban Congressional Stock Trading Act (S. 3494).

Under the Ethics in Government Act, the trustee is authorized to send a letter advising the member that the value of one of these initial assets has fallen below $1,000, as would be the case following sale of the asset, with a copy sent to the relevant ethics committee.[2] The House of Representatives has not published much guidance on qualified blind trusts, but the Senate Select Committee on Ethics has published a sample letter for this purpose.[3] A Senate model qualified trust agreement includes a provision that requires a trustee to send copies of the letter to the trust's grantor, the U.S. Senate Select Committee on Ethics, and the Secretary of the Senate.[4] The problem with this arrangement is that it gives the member greater knowledge than the public has with regard to the holdings of the trust. If the member has not received this notice of a sale, the member knows that any asset initially placed in the trust remains in the trust. Under the current system, the public is in the dark about the member's conflict of interest with known assets of the trust.

The Ban Congressional Stock Trading Act addresses this problem by requiring the relevant ethics committee to receive a copy of the notice of a sale and post it on the committee's website for public viewing.[5] As a result, the bill would put the public on an equal footing with respect to the member's holdings. Hopefully, this public awareness of any conflicts of interest would also create at least some pressure on a member to direct the trustee to divest all assets initially placed in the trust. Existing law would allow the member to issue such a direction, provided that a copy of the communication is provided to the relevant ethics office.[6]

c. Is an "informal" blind trust where a third party manages the investment portfolio of the Member, and both the Member and the trust manager attest under penalty of perjury that no information on trades will be exchanged a viable alternative?

---

[2] 5 U.S.C. app. § 102(f)(4)(A).

[3] Senate Select Committee on Ethics, "Qualified Blind Trusts," at 18, September 2015, https://www.ethics.senate.gov/public/_cache/files/286a4cf9-5aab-40ef-9a6c-bf2278e79e38/qualified-blind-trusts-guide---october-2020.pdf.

[4] Senate Select Committee on Ethics, "Qualified Blind Trusts," at 6, September 2015, https://www.ethics.senate.gov/public/_cache/files/286a4cf9-5aab-40ef-9a6c-bf2278e79e38/qualified-blind-trusts-guide---october-2020.pdf.

[5] S. 3494, "Ban Congressional Stock Trading Act" 117th Congress, section 2 (section 202(f)(1)(A)(iii) and (f)(2)(A)(ii) of the language amending the Ethics in Government Act), https://www.congress.gov/bill/117th-congress/senate-bill/3494/text.].

[6] 5 U.S.C. app. §102(f)(3)(C)(vi)(III), (E).

Response to QFR 6c:

No. Sanctioning "informal" blind trust arrangements would gut the law on qualified blind trusts by creating an exception that swallows the rule. The public would be in the dark about the holdings of these sham blind trusts, without any of the assurances that the Ethics In Government Act currently provides with regard to the uniformity of qualified blind trusts and the Member's lack of knowledge of trust property. This approach would also needlessly create a host of legal questions that are otherwise answered by the existing QBT statutory framework. POGO would vigorously oppose this type of approach.

Rather than weakening the existing blind trust requirements, Congress should be strengthening them. Congress has already fallen behind the executive branch with regard to the integrity of qualified blind trusts. Congress allows financial institutions, attorneys, certified public accountants, brokers, and investment advisors to serve as trustees of qualified blind trusts.[7] In contrast, the executive branch has taken a more rigorous stance by permitting only financial institutions to serve as trustees of qualified blind trusts.[8] OGE's regulations offer the following explanation for establishing stronger standards than the ones Congress has adopted:

> By the terms of paragraph (3)(A)(i) of section 102(f) of the Act, an individual who is an attorney, a certified public accountant, a broker, or an investment advisor is also eligible to serve as an independent trustee. However, experience of the Office of Government Ethics over the years dictates the necessity of limiting service as a trustee or other fiduciary to the financial institutions referred to in this paragraph, to maintain effective administration of trust arrangements and preserve confidence in the Federal qualified trust program. Accordingly, under its authority pursuant to paragraph (3)(D) of section 102(f) of the Act, the Office of Government Ethics will not approve proposed trustees or other fiduciaries who are not financial institutions, except in unusual cases where compelling necessity is demonstrated to the Director, in his or her sole discretion.[9]

Following OGE's lead, Congress should amend 5 U.S.C. app. § 102(f)(3)(A)(i) to limit eligibility to serve as a trustee of a qualified blind trust to a financial institution that meets the criteria OGE has set forth at 5 C.F.R. § 2634.405. It is time for the legislative branch to raise its standards to match those of the executive branch.

QFR 7. The hearing included discussion of the compliance costs associated with the creation and maintenance of a qualified blind trust and other impacts on filers. For example, Ranking Member Rodney Davis stated that he had been informed by a financial advisor that "most financial firms won't even take on a client for a blind trust unless they meet certain asset holdings and activity requirements." Ms. Schulp testified that, "Compliance costs for blind trusts tend to be substantial," and that it can take "multiple thousands of dollars to set one up."

---

[7] 5 U.S.C. app. § 102(f)(3)(A)(i).
[8] 5 C.F.R. § 2634.405.
[9] Note to 5 C.F.R. § 2634.405(a).

a. What is your understanding of the typical costs associated with establishing and maintaining a qualified blind trust? What is the typical range of costs for an attorney or other qualified professional to create such a trust? Once such a trust has been created, what is the typical range of annual costs for a trustee to administer the trust? For each, are these costs typically based on hourly or other similar basis, such as a percentage of the total assets managed in the trust?

b. What is your understanding of how common it is for financial firms or advisors to set minimum criteria for an individual's financial assets or financial activity to either create or manage a blind trust?

c. Ranking Member Davis also stated that, "these cost restrictions would put us in a situation where these perverse incentives might force Members to engage in more market trading in order to meet blind trust minimums and other requirements." What is your reaction to that statement?

d. In general, Members of Congress may not use official or principal campaign committee funds for personal purposes. However, they may use both types of funds to pay for certain expenses that are incurred because of their responsibilities or obligations that exist only because of their position as a federal officeholder. In the event that modified standards for deterring financial conflicts of interest for certain covered officials require covered officials in certain situations to establish qualified blind trusts, should those officials be permitted to use official funds to defray the costs of establishing or maintaining such trusts?

Response to QFR 7:

Costs and investment minimums will vary by provider, but the proposals POGO endorsed at the hearing would not require anyone to establish a blind trust. The decision to create a blind trust will be one that is made by an individual Member to avoid having to divest of a particular financial asset, meaning there would be no "obligation" to create a blind trust under the law.

The better option, from the perspectives of resolving conflicts of interest, transparency, and cost-effectiveness, would be for a Member to invest in diversified mutual funds, which would not pose conflicts of interest under the pending proposals.

The Senate Select Committee on Ethics (and presumably the House Ethics Committee) can supply exact cost information because the committee requires members who establish qualified blind trusts to disclose schedules of trustee fees to their supervising ethics office. See Senate Blind Trust Guide, at 2, 14.

QFR 8. The EIGA requires that a covered official who forms a QBT must receive the prior, formal approval of their supervising ethics office.

a. If a reform proposal permits covered officials to retain ownership or certain assets within a QBT, but a covered official has not yet received approval from their supervising ethics office to establish a QBT and has therefore not been able to place the assets in the QBT, what should happen? Should a covered official who has formally submitted a request for approval of a proposed QBT be permitted an extension a decision is rendered by the supervising ethics office, should they be required to divest the asset(s), or something else?

b. If a supervising ethics office either declines to approve a covered official's request to establish a trust or determines that certain assets may not be placed in an approved QBT, but the covered official may no longer own those types of assets, how long should the covered official have to divest themselves of the asset?

Response to QFR 8:

This question assumes a delay that is unlikely to occur. Both the Senate and House ethics committees have created model blind trust agreements that Members are required to use. As a result, the creation of the trust can be accomplished quickly because the trust agreement contains all provisions necessary for compliance with the law. The Member will not be involved in protracted negotiations with their ethics committee because use of these prescribed forms eliminates discretion and the potential for variation.

The only realistic potential for delay arises in connection with the Member's selection of a trustee. If the Member is slow to select a trustee or if the trustee is slow to demonstrate to the committee the absence of a prior relationship with the Member, any resulting delay will not be the fault of the ethics committee. But there is something Congress can do to eliminate this potential cause of delay: Congress can take POGO's recommendation in response to Question 6 to amend 5 U.S.C. app. § 102(f)(3)(A)(i) to limit eligibility to serve as a trustee of a qualified blind trust to a financial institution that meets the criteria OGE has set forth at 5 C.F.R. § 2634.405. By limiting the options to a financial institution, Congress would speed up the approval process because it will be easier for the ethics committee to complete the prior relationship check in the case of an institution than in the case of an individual.

QFR 9. At least one legislative proposal would require certain covered officials to completely divest certain covered assets within 180 days. How should such an approach address covered officials who have already gone above and beyond what the law requires of them today, by establishing and maintaining qualified blind trusts even though they are not required to do so, and who have therefore surrendered control over holdings in those trusts to an independent trustee? Should any reform proposal exclude qualified blind trusts approved by a covered official's supervising ethics office prior to a particular date?

Response to QFR 9:

The creation of a qualified blind trust eliminates the potential for insider trading, but it does not eliminate the potential for conflicts of interest until the trustee has sold initial property the Member placed in the trust. Therefore, the requirement to divest should apply to the initial property of the qualified blind trust but not to any property the trustee subsequently purchased.

QFR 10 and QFR 20: Beyond stock trading and ownership restrictions, what policy recommendations do you have to improve transparency, disclosure requirements and compliance with such requirements in the legislative branch?

Response to QFR 10 and QFR 20:

Beyond stock trading and ownership restrictions, Congress must also ensure that all penalties for noncompliance are meaningful, enforcement is as simple as possible with an opportunity for Members, acting in good faith, to come into compliance, and with transparency that enables routine public oversight. The penalties and process laid out in the Ban Congressional Stock Trading Act (S. 3494) satisfy these principles.

QFR 11. Various legislative proposals would create new statutory prohibitions on covered officials' financial activity, which could include significant penalties for a covered official based on a financial transaction executed by a family member or on behalf of a family member by a third party. Are existing provisions that provide "safe harbor" to covered officials who seek and rely on advice and guidance from their supervising ethics offices sufficient? Should additional clarifications be made to provide adequate protection to covered officials who act in reliance on such guidance? Would additional clarifications provide further incentive for covered officials to proactively seek and follow guidance from their supervising ethics office?

Response to QFR 11:

Members of Congress are in no danger of unfair disciplinary actions. The Senate Select Committee on Ethics has not sanctioned a single Senator in the last 15 years.[10] The House Ethics Committee only rarely takes action. Neither committee is transparent about its work, preferring to keep Americans largely in the dark about the conduct of the officials they sent to the nation's capital to represent them. But to the extent that Members of Congress fear consequences for their actions despite this history, the existing safe harbor provisions are adequate. The ethics committees will also continue issuing guidance documents, and their staffs can turn to the Office of Government Ethics for advice on how it has handled the much broader array of issues that arise among the 2.1 million-person federal workforce that it oversees. Mandatory training would also ensure Members of Congress have the knowledge they need to comply with the law. Members of Congress can also avail themselves of the option to seek individualized guidance from the committees. The desire to serve the American people ethically and responsibly should be incentive enough to ensure that lawmakers seek that guidance on their own initiative.

QFR 12. In some industries, certain individuals are required to disclose their intent to engage in financial transactions before a planned transaction. Ms. Schulp testified that ex ante disclosure by Members of Congress regarding upcoming planned transactions may "have some effect" in affecting public appearance and questions of impropriety in trading activity, and that associated burdens on the covered official "should be lighter than a blind trust or a forced sale."

a. What are your views on whether modifying the existing disclosure regime to require ex ante disclosure by covered officials would improve public confidence in the actions of their covered officials and mitigate concerns that such officials might be acting with the benefit of inside information?

---

[10] Chris Marquette, "Senate Ethics has not sanctioned a member in 14 years," *Roll Call*, February 1, 2021, https://rollcall.com/2021/02/01/senate-ethics-has-not-sanctioned-a-member-in-14-years/.

b. Could an ex ante financial transaction disclosure requirement complement other proposed reforms and provide covered officials with an additional option besides forming a qualified blind trust or divestiture?

Response to QFR 12:

This statement about Ms. Schulp's testimony on insider trading takes her remark out of its full context. Her remark must be viewed in the context of the position she articulated in her testimony that insider trading prohibitions harm the market: "Moreover, limiting the flow of information to the market from any particular subset of traders has the potential to harm market efficiency. Prohibitions on insider trading already have this effect by preventing a stock's price from reflecting all of the information known about the stock."[11] In contrast, POGO – and hopefully every Member of the committee – takes the position that insider trading harms the free market in America. This response is grounded in that fundamental position.

While advance notice of trades may, in some limited circumstances, reduce the appearance of insider trading, it will not do so in all cases. The public has no way of knowing what information a Member of Congress has received in confidential government briefings or in the course of negotiations over legislation, and there is no guarantee that a 30-day, 45-day, or 90-day advance notice period would be sufficient to ensure that the information has become widely known by the public before the Member executes a trade. As a result, advance notice of trade would not alleviate the public's concerns that a Member may be engaging in insider trading.

Moreover, advance notice of trades will have no effect whatsoever on a Member's conflicts of interest. If a Member casts a vote that benefits the Member's personal financial interests but harms the public, it will be no consolation that the Member gave advance notice of the creation of this destructive conflict of interest.

QFR 13. You testified about current practice in the executive branch with respect to divestiture, and stated that "for the most part, most individuals going in, who are subject to very similar restrictions in the executive branch, choose to divest." Mr. Straus testified that in the executive branch, Designated Agency Ethics Officers have a range of options or remedies or tools to propose addressing a covered official's financial conflict of interest, including recusal, creation of a qualified blind trust, divestiture, and others.

a. Does the Office of Government Ethics provide statistical information about the usage of these tools? For example, is data available about how many covered officials used each of those tools in a particular year?

Response to QFR 13a:

[11] Jennifer J. Schulp, "Testimony Before the Committee on House Administration Hearing on 'Examining Stock Trading Reforms for Congress,'" Cato Institute, April 7, 2022, https://docs.house.gov/meetings/HA/HA00/20220407/114485/HHRG-117-HA00-Wstate-SchulpJ-20220407.pdf.

The executive branch ethics program covers uniformed military officers and 2.1 million civilian federal employees. Given the size of the vast workforce, the Office of Government Ethics (OGE) does not have detailed information on all conflicts of interest for all employees. Nevertheless, OGE's official website includes a section for accessing ethics records of thousands of high-level officials and a separate section for accessing ethics records of agencies.

The ethics records for individuals include copies of ethics agreements signed by presidential nominees for Senate-confirmed (PAS) positions. The Senate also receives these ethics agreements as part of the nomination process. These ethics agreements are largely standardized and are based on OGE's Guide to Drafting Nominee Ethics Agreements, which supplies standard clauses for a wide variety of scenarios. These clauses are representative of the way OGE and agency ethics officials resolve conflicts of interest throughout the executive branch. (Most officials below the PAS level do not ordinarily enter into written ethics agreements, but the steps described in the clauses in OGE's guide are the same steps that those lower-level officials take to address conflicts of interest.)

The section on ethics records for agencies includes two documents relevant to this question. It contains Program Review reports, which assess individual agency ethics programs and includes a section titled "Conflict Remedies." They also contain responses from agencies to OGE's Annual Agency Ethics Program Questionnaire. OGE has posted the raw responses for all agencies on its website each year dating back to 2015. As spelled out in OGE's Program Advisory for the 2020 questionnaire (the most recent one for which OGE has posted agency responses), agencies supply data on a number of specific conflict of interest remedies and enforcement activities, including:

- Number of notification statements of negotiation or recusal under section 17(a) of the STOCK Act submitted to the ethics office in 2020 (see 5 C.F.R. 2635.602(a));
- Number of 18 U.S.C. section 208 waivers granted in 2020;
- Number of disciplinary actions taken in 2020 based wholly or in part upon violations of the Standards of Conduct provisions (5 C.F.R. part 2635) or your agency's supplemental Standards (if applicable).
- Number of disciplinary actions taken in 2020 based wholly or in part upon violations of the criminal conflict of interest statutes (18 U.S.C. sections 203, 205, 208, and 209), failure to file or filing false public financial disclosures (5 U.S.C. app. section 104 or 18 U.S.C. section 1001), a civil matter involving outside earned income (5 U.S.C. app. section 501), or outside activities (5 U.S.C. app. section 502).
- Number of referrals made in 2020 to the Department of Justice of potential violations of the conflict of interest statutes (18 U.S.C. sections 203,205, 207, 208, 209), failure to file or filing false public financial disclosures (5 U.S.C. app. section 104 or 18 U.S.C. section 1001), a civil matter involving outside earned income (5 U.S.C. app. section 501), or outside activities (5 U.S.C. app. section 502).
- Section 3 of Executive Order 13770 provides a waiver mechanism for the restrictions contained in the Ethics Pledge. Indicate below how many waivers were granted to appointees in your agency in 2020, the names of these individuals granted waivers in 2020, and which of the Pledge paragraphs were implicated.

b. What appeals or waiver options are available to an official in the executive branch for whom a DAEO recommends divestment of a particular holding?

Response to QFR 13b:

This question appears to reflect a misconception. An agency DAEO is not limited merely to *recommending* divestiture as the remedy for a conflict of interest. OGE's regulations give the DAEO authority to direct divestiture upon a finding that a financial interest poses a substantial conflict of interest, and there is no mechanism for appealing an order directing an employee to divest. 5 C.F.R. § 2635.403(b).

QFR 14. You testified that one approach with respect to divestiture for Members of Congress would be to follow the current system for executive branch officials with respect to the tax consequences for such divestitures, which "wouldn't give them a benefit and wouldn't give them a tax penalty," and would simply, "maintain their status quo until after government service, and then they would have to pay whatever taxes they would have had to pay on those assets." Similarly, Professor Nagy testified that, "if someone sells assets, sells stock and other securities because they are ordered to do so, and they move that into a diversified mutual fund, the law should be written so that capital gains [tax] is deferred."

a. If Congress were to mandate divestiture of all holdings in certain types of assets for certain covered officials – as opposed to the individualized review currently performed in the executive branch to assess whether divestiture is necessary, in which case a certificate of divestiture may be issued – would it make sense to provide similar tax treatment for all such mandated divestitures?

Response to QFR 14a:

This question contains a misconception about the executive branch. In many cases, the government conducts an individualized review of an official's holdings, pursuant to 5 C.F.R. § 2635.403(b), (c); however, there are also blanket restrictions as a matter of law, regulation, and policy that apply to categories of employees.

As a matter of policy, the Department of Health and Human Services bars all Senate-confirmed appointees from investing directly or through subsidiaries, in the following industries: (1) research, development, manufacture, distribution, or sale of pharmaceutical, biotechnology, or medical devices, equipment, preparations, treatment, or products; (2) veterinary products; (3) healthcare management or delivery; (4) health, disability, or workers compensation insurance or related services; (5) food and/or beverage production, processing or distribution; (6) communications media; (7) computer hardware, computer software, and related internet technologies; (8) wireless communications; (9) social sciences and economic research organizations; (10) energy or utilities; (11) commercial airlines, railroads, ship lines, and cargo carriers; or (12) any sector mutual fund or sector exchange-traded fund that concentrates its portfolio in any single country other than the United States.[12]

Likewise, the Senate Armed Services Committee has long barred all Senate-confirmed presidential appointees in the Department of Defense from investing in defense contractors, though the committee holds its own members to a lower ethical standard and does not bar them from investing in defense contractors.[13] This is no insignificant restriction, inasmuch as the department estimates there are over 50,000 defense contractors.[14]

The following laws and regulations also impose investment restrictions on entire classes of executive branch employees: 10 U.S.C. § 988; 12 U.S.C. § 11; 12 U.S.C. § 244; 15 U.S.C. § 2053(c); 18 U.S.C. § 440; 30 U.S.C. § 6; 30 U.S.C. § 1211(f); 31 U.S.C. § 329; 43 U.S.C. § 11; 5 C.F.R. § 3101.108; 5 C.F.R. § 3201.103; 5 C.F.R. § 3401.102; 5 C.F.R. § 3501.104; 5 C.F.R. § 4101.103; 5 C.F.R. § 5001.102; 5 C.F.R. § 5501.104; 5 C.F.R. § 5601.102; 5 C.F.R. § 5801.102; 5 C.F.R. § 6001.104; 5 C.F.R. § 6401.102; 5 C.F.R. § 6801.103; 5 C.F.R. § 8301.103; 5 C.F.R. § 8301.107; 5 C.F.R. § 8401.102; 5 C.F.R. § 9001.104; 5 C.F.R. § 9401.106; and 17 C.F.R. § 140.735-2a. (Note: this list is longer than the list included in response to QFR 1, but it is also probably an incomplete list of all such restrictions.)

With that error corrected, the answer to the question is yes, if the Certificate of Divestiture program is modeled on the one that applies to the executive branch as intended solely to alleviate the tax burden for coming into compliance with a requirement to divest. In that case, it would make sense to provide similar tax treatment for all such mandated divestitures. But the law should also limit the rollover property ("permitted property") to government bonds and diversified mutual funds (rather than any "widely held" investment fund, which would include any number of private equity funds), as the executive branch's regulations do at 5 C.F.R. § 2634.1003.

b. If a reform regime provides covered officials with a choice – e.g. requiring that for certain types of assets, covered officials either divest or place them in a qualified blind trust – would such tax treatment also be appropriate?

---

[12] See Ethics Agreement of Xavier Becerra, Secretary, Department of Health and Human Services, January 17, 2021, https://extapps2.oge.gov/201/Presiden.nsf/PAS+Index/CE0277A08063FA3A852586630031837F/$FILE/Becerra,%20Xavier%20%20finalEA.pdf. See also Ethics Agreement of Andrea Palm, Deputy Secretary, Department of Health and Human Services, February 4, 2021, https://extapps2.oge.gov/201/Presiden.nsf/PAS+Index/D9C8CD57A07A72148525868A0032D927/$FILE/Palm,%20Andrea%20%20finalEA.pdf.

[13] Warren Rojas, Camila DeChalus, Kimberly Leonard, and Dave Levinthal, "15 lawmakers who shape US defense policy have investments in military contractors," *Insider*, December 13, 2021, https://www.businessinsider.com/congress-members-are-trading-defense-stocks-while-shaping-military-policy-2021-12. Scott Higham, Kimberly Kindy, and Dan Keating, "Senate panel ban on stock for appointees but not itself seen as double standard," *Washington Post*, December 18, 2010, https://www.washingtonpost.com/politics/senate-panel-ban-on-stock-for-appointees-but-not-itself-seen-as-double-standard/2012/02/06/gIQAGA6euQ_story.html.

[14] Congressional Research Service, "Defense Primer: Department of Defense Contractors," December 19, 2018, https://crsreports.congress.gov/product/pdf/IF/IF10600/4#:~:text=As%20of%20October%202018%2C%20USCENTCOM,Afghanistan%2C%20Syria%2C%20and%20Iraq.

Response to QFR 14b:

A Certificate of Divestiture permits deferral of tax on capital gains. If there is no sale, there are no capital gains to defer.

c. Should such tax treatment be afforded to Members-elect, such as after they receive a certificate of election, to provide additional time for newly elected Members to divest applicable holdings before they are sworn in?

Response to QFR 14c:

No. Congress has not allowed the executive and judicial branches to issue Certificates of Divestiture to appointees after their Senate confirmation but before their appointment to a government position, and Congress should not give preferential treatment to Members-elect. There is always a danger that a Member-elect will not ultimately take office and become subject to divestiture requirements.

QFR 15. With respect to spouses of covered officials who may receive compensation in the form of stock grants or options, Mr. Sherman testified that "most of the proposals under consideration right now would allow for the spouses to be compensated in the way that their employers decide."
a. In your view, should there be any restrictions for covered officials whose spouses receive compensation from business activity, such as by serving on a board of directors, in the form of stock options or grants? Or should spouses in such situations be permitted to continue receiving compensation in the form of stock, provided that it is publicly disclosed?
b. Should the same answer apply in the case of a spouse who serves on the board of directors of multiple entities and receives compensation in the form of stock grants or options from multiple entities?

Response to QFR 15:

A limited exception for spouse's employment compensation may be reasonable if the spouse cannot easily negotiate a flat-rate salary or fee during the period of the Member's service in Congress. Even in the case where a Member's spouse serves on several boards, the number of companies that would qualify for this exception would be far fewer than the number of companies that a Member or a Member's spouse would otherwise be prohibited from investing in. Therefore, the impact of a narrowly crafted exception for spousal employment income would not gut a broad prohibition on investments in individual companies.

QFR 16. As shown at the hearing and in news reports, despite the existence of disclosure requirements, a number of covered officials have failed to comply with them. With respect to compliance and enforcement, you testified that, "the high-level principles to consider with an enforcement mechanism" include that "any penalties would be meaningful, that it would be easy and simple to apply, and that the public can have confidence that it is being applied evenly across the board," and "there has to be some transparency there." Similarly, Ms.

Schulp testified that, "It is worth examining whether the penalty framework is sufficiently deterrent and considering public reporting of delinquent disclosure."

a. What are reasonable additional penalties that Congress should consider that would promote compliance and provide a more meaningful penalty for violations?

Response to QFR 16a, QFR 16c, and QFR 16e:

The penalties and process laid out in the Ban Congressional Stock Trading Act (S. 3494) are reasonable and satisfy the principles POGO has laid out for Congress. That bill would allow the supervising ethics office to impose a civil penalty, equal to one month's salary, on a Member of Congress 30 days after written notification of a violation. The penalty would continue for each month the Member remains out of compliance.

b. What specific suggestions do you have for reforming the existing penalty framework?

Response to QFR 16b and QFR 16d:

Changes to the existing penalty framework under the STOCK Act would be wholly inadequate to address the problems at issue. Instead, POGO has urged Congress to combine provisions of the TRUST in Congress Act (H.R. 336), the Ban Congressional Stock Trading Act (S. 3494), and the Bipartisan Ban on Congressional Stock Ownership Act of 2022 (introduced in the House as H.R. 6678 and in the Senate as S. 3631). The ban on ownership in H.R. 6678/S. 3631 could apply to the subset of interests currently covered under that bill, and the broader definition of "covered investments" in H.R. 336 and S. 3494 could apply to assets required to be placed in a qualified blind trust, with the additional disclosure requirements of S. 3494. The enforcement provisions in these bills should also be included in the combined bill.

c. Should penalties be set at the same level for all violations, or should penalties be connected in some way to the dollar value of reportable items that were not reported in compliance with the law?

Response to QFR 16c:

See the response to QFR 16a, QFR 16c, and QFR 16e, above.

d. Should the length of tardiness of an outstanding public disclosure required by the law be a factor in the size of the penalty?

Response to QFR 16d:

See the response to QFR 16b and QFR 16d, above.

e. **Should the size of the penalty be determined in part by the number of prior violations by a covered official?**

Response to QFR 16e:

See the response to QFR 16a, QFR 16c, and QFR 16d, above.

QFR 17. Mr. Sherman testified that the ranges or intervals used for reporting various items – which can be large and even open-ended for the most substantial items – "could probably use a little bit of work." Under current law, a filer can report an asset, transaction, or liability as being worth more than $50 million, income associated with a particular asset as being worth more than $5 million, without having to provide any greater detail.

a. Do you have specific suggestions for adjusting the reporting intervals to provide greater transparency, particularly with regard to the largest items filers must disclose?
b. At least one legislative proposal would require filers to provide an estimate, rounded to an appropriate nearest amount (e.g. nearest $10,000, $100,000, or $1,000,000). Would requiring filers to provide an estimated value for reportable items in the highest value, currently open-ended intervals, improve transparency?
c. CREW, for one, has also previously identified in its work the fact that filers can use an open-ended interval that provides even less detail for assets, transactions, or liabilities which are solely owned or in the name of a filer's spouse or dependent child. For those items, a filer can report them as simply being worth more than $1 million – with no additional detail. What public policy purpose does this provision serve? Is it outdated? Should it be reformed?
d. What complications exist for requiring the exact dollar amount of a trade, if any?

Response to QFR 17:

The requirements for reporting high-value assets should be strengthened. The current high-end categories for reporting value are:

- greater than $1,000,000 but not more than $5,000,000;
- greater than $5,000,000 but not more than $25,000,000;
- greater than $25,000,000 but not more than $50,000,000; and
- greater than $50,000,000.

In the case of the spouse of a filer, these categories are compressed into a single category that identifies value as greater than $1 million.

The current law allows filers to report income in categories, but only if the income is in the form of dividends, rents, interest, or capital gain. Filers must report the exact amount of any other type of income (e.g., LLC distribution, partnership share, consulting fees, etc.). The high-income categories for dividends, rents, interest, and capital gain are:

- greater than $1,000,000 but not more than $5,000,000, or
- greater than $5,000,000.

We propose the following reforms:

In all cases, including the case of a spouse's assets, the filer should be required to report any asset worth more than $5 million by rounding the value to the nearest $5 million dollar increment. In the case of income, the filer should be required to report any income in the form of dividends, rents, interest, and capital gain exceeding $1 million by rounding the value to the nearest $1 million dollar increment. Filers should continue to report the exact amount of other types of income.

We also propose changing the requirement for the reporting of income from publicly traded investments, such as securities traded on a national exchange, mutual funds, and exchange-traded funds. Information about income in the form of dividends, rents, interest, and capital gain from these publicly traded investments is not normally needed to analyze conflicts of interest or suspicious payments; however, the reporting of this information takes considerable time and effort, diverting resources the government ethics program could apply to focusing on more significant forms of income or potentially conflicting investments. An exception could alleviate this resource drain by eliminating the requirement to report income in the form of dividends, rents, interest, and capital gain in the limited case of publicly traded investments. To close a possible avenue for bribery, the exception would not apply if the individual sold a publicly traded investment for more than market value.

QFR 18. Various proposals introduced to date include a wide range of effective dates, by which covered officials would be subject to new restrictions or requirements – whether those are divestment, creation of qualified blind trusts, or new limitations or prohibitions on certain types of financial activity.
a. What is a reasonable range of possible effective dates for any of these types of new possible requirements?
b. Does it make sense to provide for different effective dates for different requirements? For example, if a reform measure limits the types of transactions covered officials may engage in, would it make sense to provide an earlier effective date for prohibitions to engage in new purchases, while providing more time for covered officials to engage in sales transactions to divest of covered assets they already own, whether those divestments are voluntary or mandatory?

Response to QFR 18:

Ideally, the law would apply immediately. However, the effective date when current members must divest conflicting assets matters less than the effective date for new members. Any delayed implementation for current members will eventually come to an end when either the delay ends, the Members divest, or the Members are replaced by individuals who are willing to live up to higher ethical standards. But a delay applicable to new Members would be a permanent impediment to implementation, with delays being renewed at the beginning of every Congress.

There would be no excuse to delay a prohibition on acquiring new assets.

QFR 19. Are there any officials in the legislative branch who do not currently file financial disclosures or other conflicts of interest disclosures who should do so in the future?

The applicability of financial disclosure requirements to congressional staffers is generally the same as it is for rank-and-file executive branch employees.[15] (The one exception is that any Member who does not employ a staff member who meets the reporting threshold must designate at least one staffer to file publicly.)[16] The problem does not lie in the designation of which congressional staffers must apply. The problem lies in the efforts of the ethics committees to make it difficult for the public to access the disclosures of these employees. POGO's understanding is that the committees currently require the public to visit Congress in person during limited hours on certain days of the week, refuse to let the public print copies of the disclosures, and offer only a small number of computers to access these disclosures. The committees have made a farce out of the public availability of these records. Given this behavior, Congress should now mandate that all disclosures by congressional staffers be placed online for public viewing. Anything less is a decision to create only the illusion of public disclosure by these staffers.

QFR 20. Beyond stock trading and ownership restrictions, what policy recommendations do you have to improve transparency, disclosure requirements and compliance with such requirements in the legislative branch?

See response to QFR 10 and QFR 20 above.

QFR 21. Some critics of imposing restrictions on stock trading and ownership on Congress argue that such restrictions would be a cumbersome financial burden, particularly for middle class Members of Congress, especially given the costs of establishing a qualified blind trust, and that reforms should focus on improving disclosure and transparency. They argue that Members of Congress who are not independently wealthy will be disadvantaged by such restrictions. What is your perspective on this argument?

The claim that these bills would impose an undue or disproportionate burden on middle class members of Congress is untrue. There would be no requirement to create a blind trust under any of the pending bills. Middle class members of Congress rarely, if ever, hold exotic investments. For the most part, they hold mutual funds that pose no conflicts of interest and would be permitted under all of the pending bills. If they hold stocks at all, they generally hold publicly traded stocks, which are easy to divest.

As proof of the ease of compliance with these requirements, there are currently no blind trusts in the executive branch despite the fact that numerous wealthy presidential appointees have served in the current and past presidential administrations. The reason there are no blind trusts is that these appointees – wealthy and middle class alike – prefer instead to receive Certificates of Divestiture and roll the proceeds of the sale of conflicting assets into nonconflicting diversified mutual funds. The Senate has long been satisfied with this approach, which is spelled out in the ethics agreements of presidential nominees for Senate-confirmed positions. Opposition has only lately arisen because Members of Congress are finally being asked to hold themselves to the same ethical standards to which they have long held others.

[15] Compare 5 U.S.C. app. § 101(f)(3) with 5 U.S.C. app. §§ 101(f)(10) and 109(13).
[16] 5 U.S.C. app. § 109(13).

Minority questions for Ms. Hempowicz

- How would Congress enforce a complete ban on trading? Isn't it possible that such a ban would be overbroad, allowing bad actors to skirt the system more easily and punishing Members that already act in good faith?

Response:

If Congress takes POGO's proposal, the law would include appropriate enforcement provisions. POGO has urged Congress to combine provisions of the TRUST in Congress Act (H.R. 336), the Ban Congressional Stock Trading Act (S. 3494), and the Bipartisan Ban on Congressional Stock Ownership Act of 2022 (introduced in the House as H.R. 6678 and in the Senate as S. 3631). The ban on ownership in H.R. 6678/S. 3631 could apply to the subset of interests currently covered under that bill, and the broader definition of "covered investments" in H.R. 336 and S. 3494 could apply to assets required to be placed in a qualified blind trust, with the additional disclosure requirements of S. 3494. The restrictions would not be overbroad and include numerous exceptions.

The enforcement provisions in these bills should also be included in the combined bill. The penalties and process laid out in the Ban Congressional Stock Trading Act (S. 3494) are reasonable and satisfy the principles POGO has laid out for Congress. That bill would allow the supervising ethics office to impose a civil penalty, equal to one month's salary, on a Member of Congress 30 days after written notification of a violation. The penalty would continue for each month the Member remains out of compliance.

It would not be possible to skirt the system because the public disclosure requirements will ensure that both congressional ethics committees and the public can track whether Members of Congress continue to hold conflicting investments. An added transparency requirement in the Ban Congressional Stock Trading Act (S. 3494) would ensure that the public can also track the divestiture of the initial property of any blind trust. Therefore, contrary to the concern expressed in this question, the law would not allow bad actors to skirt the system more easily and punish Members that already act in good faith.

- Please explain how a certificate of divestiture would work for covered congressional individuals.
    - How would capital gains be treated?

Response:

To fully address this question, I have framed this response in a question-and-answer format, which may be useful not only to the Members who posed this question but to a broader audience of all Members of Congress and the public:

What is a CD?

Certificates of Divestiture (CDs) enable eligible persons to defer payment of capital gains taxes when government ethics rules force them to divest property (an investment). A CD is not intended to be a perk; it lessens the burden of complying with ethics rules that don't apply to the public. An example of a CD that OGE issued to an executive branch official is available online.

Who is eligible for a CD?

Certain federal government officials (executive branch employees, other than special government employees, and judges), their spouses, and their minor or dependent children are eligible for CDs. A special rule for trusts allows a trustee to request a CD if one of these eligible persons is a beneficiary of the trust. As a matter of policy, the Office of Government Ethics usually denies a CD to a trustee if any beneficiary of the trust is not an eligible person.

How does a CD work?

An individual must request and obtain a CD before selling the property. Within 60 days, the individual must use the proceeds of the sale to purchase Permitted Property. When the individual later sells the Permitted Property, the IRS collects a capital gains tax on both the sale of the Permitted Property and the sale of the original property.

What is Permitted Property?

Executive branch regulations define Permitted Property to mean a Treasury bond or a diversified mutual fund (including an exchange-traded fund). Tax law would allow an individual to choose a broader range of investment funds, but Congress would do well to adopt the definition that the executive branch has used successfully for decades.

How does an individual notify the IRS of the CD?

An individual files an IRS Form 8824 to defer payment of capital gains taxes. In Part IV of that form, the individual provides the CD number (which is printed on the CD), a description of the original property sold, and a description of the Permitted Property purchased.

How does the IRS eventually collect the deferred capital gains tax?

The tax code captures the gain (the increase in value derived) from the sales of both the original property and the Permitted Property by adjusting the Permitted Property's tax basis. To oversimplify a legal term, the tax basis of property is often what the taxpayer paid to acquire it. But that's not true in the case of Permitted Property. The tax basis of Permitted Property is the cost of acquiring the *original* property that the taxpayer sold before purchasing the Permitted Property. Here's a simplified example:

1. In 2000, an individual purchases ABC Company stock for $10.

2. In 2022, the individual receives a CD and sells the ABC Company stock for $100.

The individual normally would pay a tax on the $90 gain, but the CD allows the individual to defer payment of that capital gains tax until a later time.

3. Within 60 days, the individual uses the $100 to purchase XYZ mutual fund (the Permitted Property).

4. In 2040, the individual sells XYZ mutual fund for $150. The recognized gain is $140.

The tax basis of XYZ mutual fund would normally be $100 (the purchase price) and the gain would normally be $50. But the law requires an adjustment because the individual used a CD to defer gains on the sale of ABC Company stock. The individual must use the tax basis of the ABC Company stock, which is $10 (the purchase price for that stock). The individual subtracts this adjusted tax basis ($10) from the sale price of the XYZ Mutual fund ($150) to determine the gain ($140).

- Do you think that Members should also be limited from engaging in more complicated trades like swaps, options, or shorting a stock?

Response:

Yes.

QUESTIONS FOR THE RECORD RESPONSES SUBMITTED TO THE HOUSE COMMITTEE HEARING ON ADMINISTRATION HEARING ON EXAMINING STOCK TRADING REFORMS FOR CONGRESS

Donald K. Sherman
Senior Vice President and Chief Counsel
Citizens for Responsibility and Ethics in Washington (CREW)

1. Why, in your view, is it important to include financial activity or transactions of covered officials' spouses and dependent children within the scope of any new restrictions on stock trading and ownership?

It is important for any new restrictions on stock trading and ownership to extend to cover members' spouses and dependent children because members must not be permitted to simply transfer their individual assets to a close family member to circumvent the law. A carve-out for spouses and dependent children would undermine much of the purpose of the legislation and allow the conflicts of interest that result from the ownership of individual assets to remain.

In addition, Congress has already determined that the financial entanglements of government officials' spouses and dependent children can create significant conflicts of interests. That's why the criminal conflict of interest statute codified in the Ethics in Government Act and applicable to executive branch employees, specifically includes the financial interests of the employees' spouse and minor children. While it remains problematic that Congress exempted themselves from this provision, 18 U.S.C. § 208, it would be wildly hypocritical for Congress to exempt their spouses and minor children from any reforms it considers now.
***

2. Most of the introduced bills vary regarding what investments should be covered in a prohibition on trading and ownership and what should be exempted. Do you have specific policy recommendations for what specific types of covered investments should be included in any stock trading or ownership prohibition and what types of investments should be exempted?

Individual stocks, bonds, commodities, futures, and other similar financial instruments should be covered.

***

3. Should the following types of financial interests be subject to restrictions on ownership and/or trading activity? Why or why not?

At the outset, we wish to stress that any legislation attempting to address the problems posed by members of Congress owning or trading individual financial interests should be based on the principle that public service is a public trust. That means that the single, overarching focus should be the public's right to know, with certainty, that the people they choose to represent them are acting on their behalf--and not in service of their own financial interests

With that in mind, we strongly believe that members of Congress should not be permitted to own or trade any financial interest that could create an actual conflict of interest, or the appearance of a conflict of interest, with the member's official duties. We strongly support the prohibitions in Sen. Warren and Rep. Jayapal's Bipartisan Ban on Congressional Stock Ownership Act, and Sen. Ossoff and Rep. Spanberger's Ban Congressional Stock Trading Act.

a. Cryptocurrency: Yes. Cryptocurrency poses the same, if not greater, risk of potential conflicts of interest than traditional securities given their volatility and the relationship between their value and the current legal and regulatory environment.
b. Initial coin offerings (ICOs): Yes. Members shouldn't be allowed to purchase cryptocurrencies.
c. Special purpose acquisition company (SPAC): Yes. Members shouldn't be allowed to invest in securities, including those issued by a SPAC as part of a merger or acquisition.
d. Real estate investment trust (REIT): Yes. Members shouldn't be allowed to invest in sector specific funds or trusts, including REITs.
e. Options/futures: Yes. Members should not be allowed to own financial interests that are functionally the same as securities, including those created via synthetic means.
f. Commodities: Yes. Members should not be allowed to invest in commodities as they create functionally the same conflict concerns as securities.
g. Privately or closely held companies: Yes. In most circumstances, members should not be allowed to own privately or closely held companies. However, we do support a limited exception for truly small businesses.
h. Bonds: Yes. Members should not be allowed to own bonds other than U.S. Treasuries.

***

4. How should a reform proposal address holdings that covered officials may have in a privately held company that subsequently goes public?

Stock in a privately-held company that subsequently goes public should be treated no differently than other covered assets and should be divested within the timeframe mandated by Congress. We support a 180-day divestment period.

***

5. The range and complexity of modern financial instruments and holdings posed challenges for the supervising ethics offices related to interpreting and enforcing the STOCK Act. In addition, new products and investment forms are constantly emerging, such as cryptocurrency and SPACs. What latitude should supervising ethics offices have to interpret the scope of covered investments, to grant extensions of time to comply with any new ownership and/or trading restrictions, or to consider and grant waivers?

The divestiture periods proposed in introduced bills range between 90 to 180 days for most securities, and up to five years for more complicated holdings. Given these timeframes, supervising ethics officials should be able to fully implement newly-mandated divestiture requirements within the legislative timeframes established by Congress, which are consistent with and in some cases more generous than those used by the Executive Branch.

***

6. Some observers have focused on shortcomings with the existing statutory requirements for and features of qualified blind trusts (QBTs). For example, as you noted in your testimony, a filer knows what assets they put in a QBT at the time they create it, and current law requires the trustee to inform the covered official / trustor when an original trust asset is sold. You testified that, "qualified blind trusts could be a useful option if the member is required to effectuate the sale of all of the assets that would go into that trust beforehand."

    a. Would a requirement that the independent trustee dispose of any original trust assets within a certain period of time provide a meaningful improvement that could render QBTs a more effective and credible option than under current law? If so, do you have views about what deadlines for requiring sale of original trust assets might be reasonable?

Yes. Including such a requirement would result in the creation of a truly blind trust. In those circumstances, blind trusts pose no conflict of interest concern. We believe that 180 days following enactment or swearing in should provide a sufficient runway for the trustee to divest of the original assets.

b. Are there other ways that the law could be changed to make QBTs a more effective option for deterring financial conflicts of interest?

No. The QBT structure requires divestment to fully address financial conflicts of interest.

c. Is an '"informal" blind trust where a third party manages the investment portfolio of the member, and both the member and the trust manager attest under penalty of perjury that no information on trades will be exchanged a viable alternative?

No. It's unclear how this regime would be any different or better than the current rules barring insider trading.

***

7. The hearing included discussion of the compliance costs associated with the creation and maintenance of a qualified blind trust and other impacts on filers. For example, Ranking Member Rodney Davis stated that he had been informed by a financial advisor that "most financial firms won't even take on a client for a blind trust unless they meet certain asset holdings and activity requirements." Ms. Schulp testified that, "Compliance costs for blind trusts tend to be substantial," and that it can take "multiple thousands of dollars to set one up."
   a. What is your understanding of the typical costs associated with establishing and maintaining a qualified blind trust? What is the typical range of costs for an attorney or other qualified professional to create such a trust? Once such a trust has been created, what is the typical range of annual costs for a trustee to administer the trust? For each, are these costs typically based on hourly or other similar basis, such as a percentage of the total assets managed in the trust?

Blind trusts are generally bespoke contractual arrangements, so it is hard to say with clarity what the "typical" costs would be to set one up. In theory, the cost to set up a blind trust could vary widely depending on the complexity of the trust agreement, for example. Expenses associated with trustees will also vary widely depending on the total amount of the trust's assets, the trading strategy, and whether the trustee chooses to charge a flat hourly rate or a rate related to some other metric.

b. What is your understanding of how common it is for financial firms or advisors to set minimum criteria for an individual's financial assets or financial activity to either create or manage a blind trust?

Neither I nor my colleagues at CREW have any insight into this question.

c. Ranking Member Davis also stated that, "these cost restrictions would put us in a situation where these perverse incentives might force members to engage in more market trading in order to meet blind-trust minimums and other requirements." What is your reaction to that statement?

I do not believe that this is correct. Divestment remains the simplest and easiest way for members and their families to comply with a ban on their ownership and sale or stocks and other similar commodities. Furthermore, for many members investment in diversified mutual funds or exchange traded funds (ETFs) may be a more practical and affordable alternative to blind trusts.

d. In general, members of Congress may not use official or principal campaign committee funds for personal purposes. However, they may use both types of funds to pay for certain expenses that are incurred because of their responsibilities or obligations that exist only because of their position as a federal officeholder. In the event that modified standards for deterring financial conflicts of interest for certain covered officials require covered officials in certain situations to establish qualified blind trusts, should those officials be permitted to use official funds to defray the costs of establishing or maintaining such trusts?

No. In no circumstance would a member be required to set up a blind trust as the member could always simply divest of their conflicting assets and reinvest the proceeds in diversified mutual funds or ETFs.

***

8. The EIGA requires that a covered official who forms a QBT must receive the prior, formal approval of their supervising ethics office.
    a. If a reform proposal permits covered officials to retain ownership or certain assets within a QBT, but a covered official has not yet received approval from their supervising ethics office to establish a QBT and has therefore not been able to place the assets in the QBT, what should happen? Should a covered official who has formally submitted a request for approval of a proposed QBT be permitted an extension a decision is rendered by the supervising ethics office, should they be required to divest the asset(s), or something else?

In general, members should divest their assets if they aren't able to create a blind trust for whatever reason. If Congress decides to locate enforcement and management authority in the ethics committees, Congress must give the committees resources sufficient to complete their tasks within the statutory deadlines. It is hard to overstate how taxing this type of work would be on Committee staff without additional capacity. Because of that, we do not think that simply increasing funding will be sufficient for the ethics committees to take on this type of work.

b. If a supervising ethics office either declines to approve a covered official's request to establish a trust or determines that certain assets may not be placed in an approved QBT, but the covered official may no longer own those types of assets, how long should the covered official have to divest themselves of the asset?

We don't have a specific timeframe to suggest. To the extent Congress decides that it makes sense to allow the ethics committees to grant an extension for members to divest, we encourage you to keep the guiding principle--that public service is a public trust--in mind.

***

9. At least one legislative proposal would require certain covered officials to completely divest certain covered assets within 180 days. How should such an approach address covered officials who have already gone above and beyond what the law requires of them today, by establishing and maintaining qualified blind trusts even though they are not required to do so, and who have therefore surrendered control over holdings in those trusts to an independent trustee? Should any reform proposal exclude qualified blind trusts approved by a covered official's supervising ethics office prior to a particular date?

Members with trusts that are truly blind should be grandfathered in as their trusts would not pose a conflict risk. However, members with trusts that are not blind should be required to amend the trust document to direct the trustee to divest any original trust asset or any asset of which the member has become aware.

***

10. Beyond stock trading and ownership restrictions, what policy recommendations do you have to improve transparency, disclosure requirements and compliance with such requirements in the legislative branch?

The legislation must also include a penalty for violating these rules that is both clear enough that members understand precisely what will happen should they violate the law, and significant enough to serve as a comprehensive deterrent. As evidenced by recent stories of members trading on insider information, it is clear that current penalties are too low and that the "naming and shaming" of members in the media has not worked.

***

11. Various legislative proposals would create new statutory prohibitions on covered officials' financial activity, which could include significant penalties for a covered official based on a financial transaction executed by a family member or on behalf of a family member by a third party. Are existing provisions that provide "safe harbor" to covered officials who seek and rely on advice and guidance from their supervising ethics offices sufficient? Should additional clarifications be made to provide adequate protection to covered officials

who act in reliance on such guidance? Would additional clarifications provide further incentive for covered officials to proactively seek and follow guidance from their supervising ethics office?

Existing provisions that provide "safe harbor" to covered officials who seek and rely on formal, written advice and guidance from their supervising ethics offices are limited and should not be expanded. There do not need to be additional protections to covered officials who act in reliance on such guidance. In practice, members and staff often call supervising ethics offices in hopes of getting approval for conduct that they argue is technically within the rules. Unless members receive explicit written guidance from the supervising ethics office on official letterhead and signed by the chair and ranking member, there should be no safe harbor.

If Congress changes ethics rules that will likely result in more formal requests for guidance. To meet this increased demand, they should also ensure that there is adequate funding to expand the House and Senate Ethics Committee staffs. If not, doing so will only lead to frustration by members and more potential violations. Under no circumstances should Congress consider relaxing the "safe harbor" provisions to allow members, their family members or third parties acting on their behalf to rely on verbal or emailed statements from ethics committee staff regarding any new statutory prohibitions on covered officials' financial activity. Doing so would inevitably lead to ethics committee staff feeling undue pressure to provide members or their families the advice that they want to hear, and undermine consistency.

***

12. In some industries, certain individuals are required to disclose their intent to engage in financial transactions before a planned transaction. Ms. Schulp testified that ex ante disclosure by members of Congress regarding upcoming planned transactions may "have some effect" in affecting public appearance and questions of impropriety in trading activity, and that associated burdens on the covered official "should be lighter than a blind trust or a forced sale."

    a. What are your views on whether modifying the existing disclosure regime to require ex ante disclosure by covered officials would improve public confidence in the actions of their covered officials and mitigate concerns that such officials might be acting with the benefit of inside information?
    b. Could an ex ante financial transaction disclosure requirement complement other proposed reforms and provide covered officials with an additional option besides forming a qualified blind trust or divestiture?

Ex ante disclosure of sales would not solve the actual problem created by members owning and trading individual stocks and similar commodities – financial conflicts of interests. As the reporting by Business Insider and others has confirmed, a transparency based regime has not deterred trading and the conflicts of interests created as a result. In fact, members of both political parties have routinely failed to meet their reporting obligations; and there is no reason to believe that requiring reporting before a transaction will change that fact. As Professor Nagy testified, disclosure of conflicts without accountability will only further erode public faith in democracy. Ex ante disclosure once again places the burden on the public and the media to examine each members' financial disclosures and voice concerns in the hopes that corrective action is taken instead of placing the burden on members of Congress and their families to affirmatively avoid trades and other financial transactions that conflict with their taxpayer-funded jobs and constitutional duty.

***

13. Ms. Hempowicz testified about current practice in the executive branch with respect to divestiture, and stated that "for the most part, most individuals going in, who are subject to very similar restrictions in the executive branch, choose to divest." Mr. Straus testified that in the executive branch, Designated Agency Ethics Officers have a range of options or remedies or tools to propose addressing a covered official's financial conflict of interest, including recusal, creation of a qualified blind trust, divestiture, and others.
    a. Does the Office of Government Ethics provide statistical information about the usage of these tools? For example, is data available about how many covered officials used each of those tools in a particular year?

Until approximately 2018, the Office of Government Ethics reported annually on the number of Executive Branch public financial disclosure filers who took specific remedial actions to address ethics issues based on a review of information reported on their new entrant, annual or termination reports, including divestiture, resignation from outside positions, written disqualification, 18 U.S.C. 208 waivers, reassignment, and other remedial actions. *See. e.g.*, OGE's CY16 Annual Agency Ethics Program Questionnaire Results, at 22 (Q. 54 - Q. 62).

Beginning in 2019, OGE's annual questionnaire summaries provide less detailed information, but still report on the number of 18 U.S.C. § 208 and Ethics Pledge waivers granted and the number of statements of negotiation or recusal under the STOCK Act submitted to agency ethics officials. *See, e.g.*, OGE's Results From the 2019 Annual Agency Ethics Program Questionnaire, at 6-7 (Q. 25 - Q. 26 and Q. 48 - Q.49). The House and Senate ethics committees should adopt similar transparent processes.

b. What appeals or waiver options are available to an official in the executive branch for whom a DAEO recommends divestment of a particular holding?

The criminal conflict of interest statute, 18 U.S.C. § 208, which bars executive branch officials from participating in a particular matter that would affect their financial interests, includes provisions for individual waivers and regulatory waivers. OGE has issued regulatory waivers for *de minimis* financial holdings, diversified mutual funds and other financial interests that are deemed too remote or inconsequential to affect the integrity of the services provided by the official.

Individual waivers require prior consultation with OGE and may be granted only in limited circumstances if the individual's conflicting interests are not so substantial as to be deemed likely to affect the integrity of the services which the Government may expect from the official.

***

14. Ms. Hempowicz testified that one approach with respect to divestiture for Members of Congress would be to follow the current system for executive branch officials with respect to the tax consequences for such divestitures, which "wouldn't give them a benefit and it wouldn't give them a tax penalty," and would simply, "maintain their status quo until after government service, and then they would have to pay whatever taxes they would have had to pay on those assets." Similarly, Professor Nagy testified that, "if someone sells assets, sells stock and other securities because they are ordered to do so, and they move that into a diversified mutual fund, the law should be written so that capital gains [tax] is deferred."

    a. If Congress were to mandate divestiture of all holdings in certain types of assets for certain covered officials – as opposed to the individualized review currently performed in the executive branch to assess whether divestiture is necessary, in which case a certificate of divestiture may be issued – would it make sense to provide similar tax treatment for all such mandated divestitures?

    Yes, we support a certificate of divestiture regime for Members of Congress.

    b. If a reform regime provides covered officials with a choice – e.g. requiring that for certain types of assets, covered officials either divest or place them in a qualified blind trust – would such tax treatment also be appropriate?

    Yes.

    c. Should such tax treatment be afforded to members-elect, such as after they receive a certificate of election, to provide additional time for newly elected members to divest applicable holdings before they are sworn in?

    Yes.

***

15. With respect to spouses of covered officials who may receive compensation in the form of stock grants or options, you testified that "most of the proposals under consideration right now would allow for the spouses to be compensated in the way that their employers decide."

    a. In your view, should there be any restrictions for covered officials whose spouses receive compensation from business activity, such as by serving on a board of directors, in the form of stock options or grants? Or should spouses in such situations be permitted to continue receiving compensation in the form of stock, provided that it is publicly disclosed?

We support Congressional stock ban legislation that exempts stock, stock options and grants received as compensation from the primary occupation of a member's spouse. Any such compensation would continue to be subject to public reporting requirements.

b. Should the same answer apply in the case of a spouse who serves on the board of directors of multiple entities and receives compensation in the form of stock grants or options from multiple entities?

We support Congressional stock ban legislation that exempts stock, stock options and grants received as compensation from the primary occupation of a member's spouse. Because the exemption refers to the "primary occupation" of the spouse, it would not ordinarily apply to more than one entity.

***

16. As shown at the hearing and in news reports, despite the existence of disclosure requirements, a number of covered officials have failed to comply with them. With respect to compliance and enforcement, Ms. Hempowicz testified that, "the high-level principles to consider with an enforcement mechanism" include that "any penalties would be meaningful, that it would be easy and simple to apply, and that the public can have confidence that it's being applied evenly across the board," and "there has to be some transparency there." Similarly, Ms. Schulp testified that, "It is worth examining whether the penalty framework is sufficiently deterrent and considering public reporting of delinquent disclosure."

a. What are reasonable additional penalties that Congress should consider that would promote compliance and provide a more meaningful penalty for violations?

There are a number of ways to increase penalties for violations of the STOCK Act. For example, Rep. Porter and Senator Gillibrand's STOCK Act 2.0 suggests enhancing the penalties for late filing periodic transaction reports. Additionally, should Congress pass stock ban legislation, we would support subjecting violators to a penalty equal to a percentage of the value of the asset or transaction, or a flat fee, whichever is greater.

b. What specific suggestions do you have for reforming the existing penalty framework?

We would support substantially increasing the penalties for late filing of PTRs to promote compliance. For example, if violators were subject to a penalty equal to a percentage of the value of the asset or transaction, they would have a great financial incentive to comply. It's clear that the current penalties are too low and that the "naming and shaming" of members in the media have not worked.

c. Should penalties be set at the same level for all violations, or should penalties be connected in some way to the dollar value of reportable items that were not reported in compliance with the law?

In the context of a stock ban, we would support tying the penalty to the size of the asset or the trade, or a flat base fee, whichever is higher. In the context of a STOCK Act violation, we would be open to tying the fine to the amount of the trades reported in the PTR, though we believe that a flat fee would likely be easier to administer.

d. Should the length of tardiness of an outstanding public disclosure required by the law be a factor in the size of the penalty?

Yes. We believe that a penalty that increases daily or weekly would be a significant deterrent for late filing of PTRs and other STOCK Act disclosures.

e. Should the size of the penalty be determined in part by the number of prior violations by a covered official?

We would be open to increasing penalties for repeat offenders.

***

17. You testified that the ranges or intervals used for reporting various items – which can be large and even open-ended for the most substantial items – "could probably use a little bit of work." Under current law, a filer can report an asset, transaction, or liability as being worth more than $50 million, income associated with a particular asset as being worth more than $5 million, without having to provide any greater detail.

Although there is substantial room for improvement in the financial disclosure framework, we believe that Congress should give highest priority to establishing a Congressional stock ban that requires divestiture of stock, bonds and other covered securities since these holdings undermine public trust based on actual or apparent conflicts of interest and insider trading concerns.

That said, the current financial disclosure framework established under the Ethics in Government Act of 1978 ("EIGA"), 5 U.S.C. app. §§ 101-111, does not adequately address the dramatic increase in wealth experienced by many high-level government officials and the vehicles used to hold and transfer that wealth. For this reason, we have recommended amending EIGA to require filers to report:

- the value of all assets, transactions and liabilities that exceed $50 million to the nearest $100 million;
- the value of income that exceeds $5 million to the nearest $10 million; Note: This amendment would not affect the reporting requirement for specific types of income that must be reported exactly (e.g., salary income).
- for any LLC or other privately held business that is not divested, the identity and amounts received by the LLC or other privately held business from its major creditors, investors and customers; and
- for gifts that exceed $1,000 in value undertaken by the filer to comply with divestiture commitments, report on the periodic financial transaction report within 30 days of the transaction.

a. Do you have specific suggestions for adjusting the reporting intervals to provide greater transparency, particularly with regard to the largest items filers must disclose?

See answer to Q. 17 above.

b. At least one legislative proposal would require filers to provide an estimate, rounded to an appropriate nearest amount (e.g. nearest $10,000, $100,000, or $1,000,000). Would requiring filers to provide an estimated value for reportable items in the highest value, currently open-ended intervals, improve transparency?

In addition to the response provided to Q. 17(a) above, we support other Congressional efforts to enhance transparency, including estimates rounded to the nearest amount.

c. CREW, for one, has also previously identified in its work the fact that filers can use an open-ended interval that provides even less detail for assets, transactions, or liabilities which are solely owned or in the name of a filer's spouse or dependent child. For those items, a filer can report them as simply being worth more than $1 million – with no additional detail. What public policy purpose does this provision serve? Is it outdated? Should it be reformed?

To the extent that spouses are permitted to retain assets that give rise to conflicts of interest, there is a heightened need for greater transparency, which outweighs privacy interests that may have been used in the past to justify more limited disclosure requirements for spousal assets, liabilities and income.

d. What complications exist for requiring the exact dollar amount of a trade, if any?

A member's broker or financial advisor should be able to make readily available to him or her the exact dollar amount of any trade involving a publicly-held company. Nonpublic holdings may be more complicated depending on the nature and terms of how it was acquired and divested. Our experience shows that reporting capital gains is also not particularly problematic for public filers since capital gains are only required to be reported annually on May 15th, and can be easily obtained from the member's tax return, which is required to be filed on April 15th.

***

18. Various proposals introduced to date include a wide range of effective dates, by which covered officials would be subject to new restrictions or requirements – whether those are divestment, creation of qualified blind trusts, or new limitations or prohibitions on certain types of financial activity.

    a. What is a reasonable range of possible effective dates for any of these types of new possible requirements?

In general we support an upper limit of 180 days for ensuring that members come into compliance. We would also be open to allowing the enforcing body to grant a limited number of short extensions to allow members to unwind complicated positions. Additionally, we would be open to allowing members additional time to unwind positions in certain complex investment vehicles.

    b. Does it make sense to provide for different effective dates for different requirements? For example, if a reform measure limits the types of transactions covered officials may engage in, would it make sense to provide an earlier effective date for prohibitions to engage in new purchases, while providing more time for covered officials to engage in sales transactions to divest of covered assets they already own, whether those divestments are voluntary or mandatory?

We believe that having multiple effective dates would add unnecessary complexity.

***

19. Are there any officials in the legislative branch who do not currently file financial disclosures or other conflicts of interest disclosures who should do so in the future?

Reforms to the legislative branch financial disclosure process should focus primarily on members of Congress. Members are elected and have a constitutional duty to the public. Congressional staff are ultimately accountable to their employing member or office and can recuse when there is a conflict that interferes with their work or can be fired if they commit serious breaches of ethical guidelines. Rather than expanding who reports, Congress should expend resources to make member disclosures more transparent, accessible and user-friendly. Members of the media and public should be able to sort financial disclosure statements in a digital format by committee or by asset, etc. so that they can better understand how their members' financial entanglements compare to others or potentially intersect with issues they care about.

***

20. Beyond stock trading and ownership restrictions, what policy recommendations do you have to improve transparency, disclosure requirements and compliance with such requirements in the legislative branch?

We believe that Rep. Porter and Sen. Gillibrand's STOCK Act 2.0 provides a number of useful policy options for increasing transparency and compliance. For example, we would strongly encourage Congress to require that all financial disclosures be submitted in a machine readable, searchable, and downloadable format.

***

21. Some critics of imposing restrictions on stock trading and ownership on Congress argue that such restrictions would be a cumbersome financial burden, particularly for middle class Members of Congress, especially given the costs of establishing a qualified blind trust, and that reforms should focus on improving disclosure and transparency. They argue that Members of Congress who are not independently wealthy will be disadvantaged by such restrictions. What is your perspective on this argument?

This argument is not serious and should not be given any credence. There are many systemic barriers to members of the working class or middle class from serving in Congress. Placing restrictions on stock trading and ownership would not contribute to these barriers. While some argue that restrictions would be a cumbersome financial burden, those concerns ignore the fact that divestment from owning individual stocks and similar commodities is a simple and cost-effective compliance mechanism available to the overwhelming majority of members who hold these assets.

Members of Congress who are not independently wealthy are disadvantaged in lots of ways relative to their wealthier peers, but those have not and should not be an excuse to undermine ethics reform. For example, our campaign finance laws, overseen by this Committee, allow candidates to loan or spend unlimited amounts of their own funds to their political campaigns. Some members can afford to pay a private accountant to manage and fill out their financial disclosure statements. Many middle class members can't afford those services and prepare the documents themselves leading to more potential errors. The fact that some members can afford an accountant does not make the requirement to fill out financial disclosure statements unfair. There are always going to be more advantages for members who are wealthy as compared to their middle class peers. That should not and cannot be a reason for Congress to pass weaker ethical reforms than this moment demands.

The American public remains concerned that members are using their government roles to enrich themselves and that they are overseeing companies and industries where they have a significant financial stake. If using a qualified blind trust is an option for some members, investment in diversified mutual funds and ETFs or divestment remain options for members, middle class or wealthy. Congress should be focused on implementing the most significant ethical reforms it can. While concern about the collateral effects of such changes is important, including considerations of class disparities, those concerns are not apparent or valid here. Disclosure and transparency haven't worked and allowing the status quo to persist undermines the efficacy of Congress, public faith in the institution, AND would only serve to increase the class divide between wealthy and middle class members.

Questions for the Record from *Hearing on Examining Stock Trading Reforms for Congress Before the U.S. House of Representatives Committee on House Administration*

Responses from Donna M. Nagy
C. Ben Dutton Professor of Business Law
Indiana University Maurer School of Law

May 31, 2022

Question #1

You testified about the fact that some legislative proposals "seek to restrict the ownership of certain investments by Members of Congress," while "others seek to restrict only the trading of such investments during congressional service." You recommended an approach that addresses both ownership and trading, and stated that what is most needed "is a Federal statute that prohibits Members of Congress and their spouses and dependent children from owning the securities of individual, publicly traded companies." How should Congress address ownership and trading interests of covered officials in closely held and privately owned companies?

Because stock and other individual investments in publicly traded companies pose risks of both conflicts of interest and unlawful insider trading, legislative reform, at a minimum, should prohibit Members of Congress and their spouses and dependent children ("covered persons") from owning such securities. Members are in a unique position to obtain material nonpublic information that could be used surreptitiously for securities trading purposes, and their legislative activities directly and substantially affect the market value of the companies in which they own shares. But even if Members are not influenced by their investments when they sponsor, oppose, or vote on legislation, and are not trading on the basis of nonpublic government information, their mere ownership of securities in publicly traded companies contributes to a corrosive belief that lawmakers *can* place their personal financial interests ahead of the public they serve..[1]

Equity interests in closely held and other privately owned companies also can be highly problematic, at least from a conflict-of-interest perspective. Controlling interests in businesses likely to be directly and substantially affected by legislation in highly regulated sectors such as energy, defense, health care, and financial services present a particular risk of conflicts, as do businesses that raise capital, borrow money, or otherwise operate overseas.

The lack of transparency surrounding hedge funds and private equity funds likewise undermines public confidence in the Members who own shares in such funds. The fact that investments in the funds are reported on a Member's public financial

[1] See Donna M. Nagy, *Owning Stock While Making Law: An Agency Problem and a Fiduciary Solution*, 48 WAKE FOREST LAW REVIEW 567 (2013). I have included this article as an attachment to my QFR responses.

disclosure forms is of little benefit when there is no publicly available information about the funds' underlying assets.

Thus, legislative reform should also require covered persons to divest most investments in business entities even when they are not publicly traded. Exceptions could be made to allow covered persons to own, through corporate entities or otherwise, family-owned farms and some other local businesses.

Of the bills I have reviewed, the *Bipartisan Ban on Congressional Stock Ownership Act of 2022* (H.R. 6678, introduced by Representatives Jayapal and Rosendale; S. 3631, introduced by Senators Warren and Daines) best balances the need for comprehensive conflict-of-interest reform with the reality that many Members and their immediate families hold investments in privately owned entities that may warrant individualized treatment. The proposed legislation enumerates several exceptions to what is otherwise a broad provision that prohibits Members and their spouses from owning an interest in or trading (except as a divestment) "any stock, bond, commodity, future, or other form of security, including an interest in a hedge fund, a derivative, option, or other complex vehicle.".[2] The exceptions include:

- an investment fund that is widely held and diversified, and does not present a conflict of interest;
- U.S. Treasury bills, notes, or bonds;
- securities received as compensation from the primary occupation of a spouse; and
- an interest in a "small business concern," as that term is defined in section 3 of the Small Business Act (15 U.S.C. 632), provided the small business concern does not present a conflict of interest..[3]

Responsibility for issuing "interpretive guidance" would fall upon the Committee on Ethics of the House of Representatives and the Select Committee on Ethics of the Senate,.[4] and presumably those Committees would undertake to determine, on a case by case basis, whether a Member must refrain from certain legislative activities (such as sponsoring legislation or committee participation) to mitigate a conflict that would otherwise be present because of an interest in a "small business concern" or in a spouse's compensation-related securities that qualify for an exception.

The bill also sets reasonable timeframes for the requisite divestments: for current Members and their spouses, most prohibited assets must be divested within 180 days of

[2] *Bipartisan Ban on Congressional Stock Ownership Act of 2022*, H.R. 6678/S. 3631 at § 2(b)(1), 117th Cong. (2022). The bill does not, however, extend the prohibition to dependent children of Members. But other bills define covered persons to include dependents. See *Ban Congressional Stock Trading Act*, S.3494, 117th Cong. (2022) (extends to a child or another relative who resides in a Member's immediate household); *Trust in Congress Act*, H.R. 336, 117th Cong. (2021) (dependent child).

[3] See § 2(c) of the *Bipartisan Ban on Congressional Stock Ownership Act*, *supra* note 2.

[4] *Id.* at § 2(f).

the legislation's enactment,[5] with a five-year period for divesting an interest in a "hedge fund, venture capital fund, or other privately held complex investment vehicle.".[6]

In addition, the bill allows Members and their spouses to convert the proceeds from their sales of individual stocks and other proscribed investments into either widely held and diversified investment funds or Treasury securities while deferring any capital gains taxes until they sell those new investments..[7] Congress has previously amended the tax code to allow for the deferral of capital gains when an executive branch official converts assets into permissible investments to avoid conflicts of interest,[8] and fairness should dictate that a similar provision apply to the legislative branch.

Question #2

You testified that the Speech or Debate clause represents an obstacle to enforcement of the insider trading prohibition in the legislative branch. Can you please expand on this assertion and also on any other enforcement challenges with the insider trading prohibition in Congress?

A principal goal of the Stop Trading on Congressional Knowledge Act of 2012 was to "reassure[ ] the American people that there are no barriers to prosecuting Members and employees of Congress for insider trading.".[9] But while the Constitution's Speech or Debate Clause was discussed extensively in House and Senate hearings on the STOCK Act,[10] Congress enacted the legislation without coming to terms with the fact that the Clause would often function as a substantial barrier to executive-branch investigations and prosecutions of congressional insider trading.

Insider trading cases rarely involve a smoking gun and must generally be constructed through circumstantial evidence establishing the elements of liability under Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934. If a Member or an employee of Congress is suspected of surreptitiously trading securities on the basis of congressional knowledge, key elements of the offense would include that the official, at the time of such trading, was *aware* of information that was both *material* and *nonpublic*.

In a typical insider trading investigation, including those involving possible trading based on market-moving government information, the need to establish those three essential elements would almost certainly prompt law enforcement officials at the

[5] *Id.* at § 2(b)(2)(A)(i).

[6] *Id.* at § 2(b)(2)(A)(ii).

[7] *Id.* at § 2(e).

[8] See RICHARD W. PAINTER, GETTING THE GOVERNMENT AMERICA DESERVES: HOW ETHICS REFORM CAN MAKE A DIFFERENCE (Oxford U. Press 2009) at 42 (discussing 5 CFR 2634.1006's provision for a rollover into permitted property).

[9] 158 CONG. REC. S141 (daily ed. Jan. 30, 2012) (statement of Sen. Carl Levin).

[10] See Anne Fodor, *Congressional Arbitrage at the Executive's Expense: The Speech or Debate Clause and the Unenforceable STOCK Act,* 108 NW. U. L. REV. 607, 629-30 (2014).

U.S. Securities and Exchange Commission (SEC) or the U.S. Department of Justice (DOJ) to interview or seek testimony from not only the securities trader under suspicion but also others who might know the precise information that was disclosed to the trader as well as how and when such information was conveyed. The Speech or Debate Clause, however, insulates legislative branch officials from being "questioned in any other Place,".[11] which protects against inter-branch inquiries into "legislative acts." That term, as the Supreme Court has emphasized, has "consistently been defined as an act generally done in Congress in relation to the business before it.".[12] Legislative acts therefore extend far beyond the communication of information in actual speeches on the House or Senate floor or in congressional debates. Legislative activity also encompasses the giving and receiving of information in committee hearings[13] and in congressional briefings by executive branch officials..[14] The term "questioning" likewise has been construed broadly to apply to document subpoenas[15] and search warrants..[16]

The upshot is that the Speech or Debate Clause will often substantially impede the gathering of essential evidence by SEC or DOJ officials,.[17] even if, for example, a Member of Congress actually had purchased stock in a defense contractor based on information "learned in a closed committee meeting of plans to boost the Pentagon's budget by tens of billions of dollars," or if a Member actually had sold (or shorted) pharmaceutical stock after learning from a "Committee Chair that legislation to cut drug prices would be moving in Congress" or from "a top secret briefing that a company was facing big legal trouble.".[18] In the absence of testimonial or documentary evidence

[11] Article I, Section 6, Clause 1 of the United States Constitution.

[12] United States v. Brewster, 408 U.S. 501, 512 (1972).

[13] See Eastland v. U. S. Servicemen's Fund, 421 U.S. 491, 504 (1975) (the Clause protects activities that "are 'an integral part of the deliberative and communicative processes by which Members participate in committee and House proceedings with respect to the consideration and passage or rejection of proposed legislation'") (quoting Gravel v. United States, 408 U.S. 606, 625 (1972)).

[14] United States v. Dowdy, 479 F.2d 213, 223-24 (1973) (extending the Clause's protection to a Representative's gathering of information from a federal prosecutor and federal housing agency officials in preparation for a possible subcommittee investigatory hearing).

[15] Brown & Williamson Tobacco Corp. v. Williams, 62 F.3d 408, 420-21 (D.C. Cir. 1995) (the Speech and Debate Clause applies to situations not only in which "members or their aides are personally questioned" but also in which subpoenas seek only documents).

[16] United States v. Rayburn House Office Bldg., 497 F.3d 654 (D.C. Cir. 2007) (holding that the Clause provides a broad non-disclosure privilege for documents falling within the sphere of legitimate legislative activity, and concluding that FBI agents' search of Representative William J. Jefferson's paper files in his congressional office violated Speech or Debate Clause).

[17] See SEC v. House Committee on Ways and Means and Brian Sutter, 161 F.Supp.3d 199, 246-47 (S.D.N.Y. 2015) (holding that certain sought-after documents and aspects of testimony, which potentially related to suspicious insider trading possibly based on unannounced changes in payment rates for physicians serving Medicare patients, fell "within the 'legitimate legislative sphere'" and thus constituted information privileged from disclosure pursuant to the Speech or Debate Clause).

[18] Transcript of *Hearing on Keeping Markets Fair: Considering Insider Trading Legislation Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs* (April 5, 2022) (hypothetical questions about whether such acts could be "considered insider trading" in colloquy between Senator Elizabeth Warren and Professor and Former SEC Commissioner Robert J. Jackson, Jr.).

detailing the precise information disclosed to the Member in the course of a closed committee meeting, a conversation with a Committee Chair, or a top-secret briefing, even indisputably illegal instances of congressional insider trading could not be effectively investigated and prosecuted..[19]

But the Speech or Debate Clause is not the only enforcement challenge involving the insider trading prohibition in Congress..[20] In a civil prosecution, the SEC would need to establish the "nonpublic" and "materiality" elements of the Rule 10b-5 offense by a preponderance of the evidence, and in a criminal prosecution, the DOJ must prove its case beyond a reasonable doubt. Information is considered "nonpublic" if it is not generally available to the investing public. That is, information becomes public when it has been disclosed "to achieve a broad dissemination to the investing public generally".[21] or when, although it is known only by a few persons, their trading on the basis of it "has caused the information to be fully impounded into the price of the particular stock.".[22] These legal standards for determining whether congressional knowledge that is traded upon is in fact "nonpublic" will pose particular difficulties given that, as guidance from the Senate Select Committee on Ethics acknowledges, "a great deal of Congressional work is conducted in the public record" at least technically, or is officially "in the public realm during [open] committee hearings, and markups, floor activity, and speeches.".[23] Accordingly, even congressional knowledge that is technically and officially "public" can remain unknown to the "investing public generally" or might not yet be "fully impounded into the price" of shares in a company substantially affected by legislative activity.

Establishing the "materiality" of any congressional knowledge that was traded upon would present another unique hurdle. Information is considered "material" if "there is a substantial likelihood" that a reasonable investor "would consider it important" in making an investment decision..[24] Moreover, when information is "soft" or contingent, its materiality is to be judged by "a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event" in light of the totality of facts and circumstances..[25] Yet, notwithstanding the breadth of these definitions, both courts and

---

[19] If, however, a Member were suspected of sharing nonpublic congressional knowledge with an individual outside of Congress for securities trading purposes, the SEC could subpoena that third party to seek information establishing what the Member disclosed (and therefore possessed at the time of the suspicious trading). See Christian Berthelsen, *Senator Burr's Brother-In-Law Ordered to Testify About Covid Stock Trades*, BLOOMBERG (Nov. 10, 2021) (reporting that "[t]he SEC is investigating whether sales were informed by classified briefings about the virus that Burr received as then-chair of the Senate intelligence committee").

[20] See Donna M. Nagy, *Insider Trading, Congressional Officials, and Duties of Entrustment*, 91 BOSTON UNIV. L. REV. 1105, 1128-29 (2011).

[21] Dirks v. SEC, 463 U.S. 646, 653 n.12 (1983).

[22] United States v. Libera, 989 F.2d 596, 601 (2d Cir. 1993).

[23] See Senate Select Committee on Ethics, *Restrictions on Insider Trading Under Securities Laws and Ethics Rules* (Dec. 4, 2012), cited in Stanley M. Brand, *DOJ Drops Investigation Into Three Senators for Insider Trading, Burr Probe Continues*, THE CONVERSATION (Apr. 2, 2020).

[24] Basic Inc. v. Levinson, 485 U.S. 224, 231-32 (1988).

[25] *Id.* at 238 (quoting SEC v. Tex. Gulf Sulphur Co., 401 F.2d 833, 849 (2d Cir. 1968) (en banc)).

the SEC have recognized that securities traders should remain free to "piece seemingly inconsequential data together with public information into a mosaic," which only becomes material when the individual pieces are placed together in one picture.[26] Whether nonpublic facts learned in a congressional hearing or briefing are material, or whether such facts are merely inconsequential data contributing to a mosaic, could be a difficult question,[27] and a legal finding that nonpublic congressional knowledge was "inconsequential" would only further convince the public that congressional corruption is rampant.

The suspicion that a Member of Congress has engaged in illegal insider trading, however, will not go away simply because the SEC or DOJ's investigative process is difficult or because the legal standards that are necessary to establish Rule 10b-5 liability can be murky. The corrosive nature of these suspicions is all the more reason for Members to give up ownership of publicly traded securities while in office.

Question #3

What administrative challenges do you foresee with allowing for a qualified blind trust option for Members?

A second principal goal of the STOCK Act was to "improve[ ] congressional transparency by requiring that personal financial disclosure filings required by Members…are made available electronically to the public."[28] Indeed, emphasizing that "sunshine is the best guarantee of integrity," Senator Joseph Lieberman predicated that the public's "increased access to information about [Members'] holdings and transactions…ought to be enough to guarantee the public or to energize the public to make sure we are following the highest ethical norms."[29] But it wasn't. More than a decade and many congressional trading scandals later, the public's doubts about Congress's integrity have only intensified.

Qualified blind trusts (QBTs), however, are premised on secrecy rather than transparency. Thus, the widespread use of QBTs by Members to restore the public's confidence in Congress could trigger precisely the opposite result.

For a blind trust to be "qualified," the trust must be reviewed and certified by the House Committee on Ethics or the Senate Select Committee on Ethics, and the covered person must surrender entirely the management of assets to an independent trustee. The trustee cannot have any family or present/previous business connection with the covered person and must be solely responsible for making investment decisions for that person's benefit without that person's knowledge. The applicable rules further provide that the

---

[26] Elkind v. Liggett & Myers, Inc., 635 F.2d 156, 165 (2d Cir. 1980).

[27] See Joan Heminway, *Materiality Guidance in the Context of Insider Trading: A Call for Action*, 52 AM. U. L. REV. 1131, 1138-39 (2003) ("The facial simplicity of the basic legal standard governing materiality masks the complexities encountered by…the SEC, the [DOJ], and courts in interpreting and applying that standard").

[28] 158 CONG. REC. S142 (daily ed. Jan. 30, 2012) (statement of Sen. Carl Levin).

[29] 158 CONG. REC. S309 (daily ed. Feb. 2, 2012) (statement of Sen. Joseph Lieberman).

trustee must "be an independent financial institution, lawyer, certified public accountant, broker, or investment advisor," and prohibit communications between the trustee and the covered person subject to a few limited exceptions.[30]

Thus, when QBTs are truly blind, Members will not know of the assets in their trusts—but neither will the press nor the public. Regardless of whether Members have complied with these stringent QBT requirements, the press and the public are likely to be skeptical. And not knowing what investments are in the QBTs, and not knowing for sure whether Members secretly know what is in their QBTs, the public may assume the worst—that the stringent requirements making the QBT an effective anti-conflict device are being violated. Moreover, as we have seen in instances with other public officials, journalists and government watchdog groups can sometimes learn of the holdings in a blind trust—prompting additional concerns about conflicts of interests.[31]

There is also little reason to be optimistic about the House and the Senate's ability to adequately monitor compliance with the extremely strict requirements of so many additional QBTs. Press reports indicate that the STOCK Act's 45-day reporting requirement for securities transactions is routinely disregarded by Members with little consequence.[32] Accordingly, the additional compliance challenges that would be presented by widespread use of congressional QBTs seem immense.

*****

Thank you very much for the opportunity to share these answers for the record.

Attachment

---

[30] 5 U.S.C. § 102(f)(3). *See also* U.S. Select Committee on Ethics, *Qualified Blind Trusts* (Sept. 2015).

[31] A recent example involves Illinois Governor J.B. Pritzker. Notwithstanding the billionaire governor's creation of a blind trust, he continues to face questions regarding the propriety of his investments. See, e.g., David Jackson, *Pritzker Trust Bought Stock in a Top Illinois Contractor After He Was Elected Governor*, Bettergov.org (Feb. 25, 2022) (reporting about the trust's purchase of "stock in one of the state's biggest Medicaid contractors" and "highlighting the weakness of Pritzker's blind-trust arrangement in preventing conflicts of interest"); Mike Flannery, *Illinois Gov. Pritzker Under Fire for His 'Blind Trust' Investment with State Government*, Fox32Chicago (Feb 25, 2022) (reporting on an aide's statement that "Pritzker wasn't aware of the investment until after his trustees made it").

[32] See Dave Levinthal, *63 Members of Congress Have Violated a Law Designed to Stop Insider Trading and Prevent Conflicts-of-Interest*, BUSINESS INSIDER (May 31, 2022).

OWNING STOCK WHILE MAKING LAW: AN AGENCY PROBLEM AND A FIDUCIARY SOLUTION

*Donna M. Nagy**

INTRODUCTION

Whether the decision making occurs inside a corporate boardroom or on Capitol Hill, acts of governing precipitate agency problems. Agency theory rests on the conflicts of interest that exist when one party (an agent) has been entrusted with the discretion to make decisions that affect and bind another party (a principal).[1] Those conflicts arise in the corporate world, where shareholders entrust boards of directors to manage corporations. Those conflicts are also present in the political world, where citizens entrust politicians to manage the government. The fundamental challenges in each context lie in motivating agents to act in their principals' best interest and reducing the costs of monitoring.

Confronted with comparable agency problems, shareholders and citizens look to similar fixes. Elections, for example, motivate agents to specify ex ante how they plan to exercise their power and discretion. And, at least in theory, agents who fail to honor their promises or otherwise act unfaithfully decrease their chances of returning to service.[2] Fiduciary obligations provide another

---

* Interim Executive Associate Dean and C. Ben Dutton Professor of Law, Indiana University Maurer School of Law—Bloomington. I presented this Article at *Agency Theory: Still Viable?*, a symposium inspired by the work of Professor Michael Jensen, at Wake Forest University School of Law on March 22, 2013. I am grateful to Professor Jensen and Professor Alan Palmiter, the student editors, and my fellow symposium participants. The Article also has benefited from helpful insights and comments by Professors Kathleen Clark, Tamar Frankel, Luis Fuentes-Rohwer, Charles Geyh, Dawn Johnsen, Richard Painter, and Margaret Sachs, and from excellent research assistance by Reference Librarian Jennifer Morgan and Helen Arnold, J.D. '13.

1. Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976).

2. For an often-cited study challenging this theory, see Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675, 688 (2007) (evidencing that successful electoral challenges to incumbent directors are "quite rare" and concluding that "even when shareholder dissatisfaction with board actions and decisions is substantial, challengers face considerable

important mechanism for mitigating agency problems. This is seen in corporate law, which imposes fiduciary duties on corporate officials and allows the corporation (and sometimes its shareholders) to enforce those obligations in court. But while the idea of lawmakers as fiduciaries is hardly a new one,[3] the implementation and enforcement of fiduciary principles—most particularly the fiduciary duty of loyalty—is frequently overlooked as a meaningful supplement for the imperfect and incomplete checks on agency problems provided by legislative elections.[4]

This Article focuses on members of Congress and their widespread practice of holding personal investments in companies that are directly and substantially affected by their legislative

impediments to replacing boards"). For analysis pertaining to lawmakers, see Stephen Ansolabehere & James M. Snyder, Jr., *The Effects of Redistricting on Incumbents*, 11 ELECTION L.J. 490, 490 (2012) (observing that "[s]itting legislators, when they run for reelection, evidently enjoy substantial electoral advantages, which are manifest both in voters' behavior and in aggregate rates of electoral competition and legislative turnover").

3. *See* TAMAR FRANKEL, FIDUCIARY LAW 279 (2011) (emphasizing that private sector fiduciaries and public sector officials are governed by the same guiding principles, which are designed to "prevent misappropriation of entrustment and ensure a diligent and expert performance of services"); RICHARD W. PAINTER, GETTING THE GOVERNMENT AMERICA DESERVES: HOW ETHICS REFORM CAN MAKE A DIFFERENCE 2–4 (2009) (stating that "[p]ersons who choose elected officials are entrustors to whom officials owe fiduciary obligations" and observing that the principles of transparency and accountability in private law are equally essential to the public law regulating government officials). For law review articles recognizing that government officials are fiduciaries who operate under strict limitations when using government power and property, see, e.g., Kathleen Clark, *Do We Have Enough Ethics in Government Yet?: An Answer from Fiduciary Theory*, 1996 U. ILL. L. REV. 57 (1996); Sung Hui Kim, *The Last Temptation of Congress: Legislator Insider Trading and the Fiduciary Norm Against Corruption*, 98 CORNELL L. REV. 845 (2013); Robert G. Natelson, *The Constitution and the Public Trust*, 52 BUFF. L. REV. 1077 (2004); D. Theodore Rave, *Politicians as Fiduciaries*, 126 HARV. L. REV. 671 (2013).

4. *See* PAINTER, *supra* note 3, at 5 (observing that corporate managers and government officials share "the power of incumbency," and bemoaning that, "[i]n both contexts, poorly performing fiduciaries are often hard to get rid of"). For additional commentary highlighting the agency problems common to corporate and public governance, see, e.g., Claire Hill & Richard Painter, *Compromised Fiduciaries: Conflicts of Interest in Government and Business*, 95 MINN. L. REV. 1637 (2011) (analyzing the 2008 government bailout of financial institutions and encouraging greater attention to structural biases in future decision making concerning the economy); Samuel Issacharoff & Richard H. Pildes, *Politics as Markets: Partisan Lockups of the Democratic Process*, 50 STAN. L. REV. 643 (1998) (envisioning a greater role for courts in reviewing political arrangements that entrench incumbents and thwart challengers); Rave, *supra* note 3 (examining the practice of gerrymandering and proposing that redistricting plans be subject to either voter ratification or judicial review for "entire fairness").

activity. Whether entirely accurate or not, congressional officials with investment portfolios chock-full of corporate stocks and bonds contribute to a corrosive belief that lawmakers can—and often do—place their personal financial interests ahead of the public they serve. This classic agency problem has been depicted in front-page news stories with jarring headlines.[5] But despite the media attention and an all-time low in public approval ratings, members of Congress continue to own and actively trade securities totaling hundreds of millions of dollars in companies directly impacted by legislative actions. Beyond that, the membership of many congressional committees holds disproportionately large investments in the industries and companies subject to their oversight.[6]

Such blatant conflicts of interest constitute standard congressional fare because the federal financial conflict statutes guarding against self-interested decision making by executive and judicial branch officials do not apply to Congress. To be sure, both the Senate and the House of Representatives have ethics rules that prohibit members from deriving personal financial gain from their congressional service. But long-standing interpretations of those rules allow lawmakers to work on and vote on legislation impacting their own personal investments provided they are not the sole beneficiaries of that legislation (or part of a highly circumscribed class of beneficiaries). This sole/limited beneficiary gloss insulates lawmakers from the fiduciary principles that would otherwise operate to restrict their personal investment practices. The federal government's recent and unprecedented involvement with financial markets and private-sector businesses (such as banks, health care providers/insurers, and automobile manufacturers), and the sheer

5. Journalists from the *Washington Post* have provided the most extensive reporting to date. *See, e.g.*, Scott Higham et al., *Senate Panel Ban Seen as Double Standard*, WASH. POST, Dec. 19, 2010, at A1; Paul Kane, *Lawmakers Reveal Health-Care Investments*, WASH. POST, June 13, 2009, at A1; Dan Keating et al., *Legislators Traded Millions in Stocks They Could Impact*, WASH. POST, June 24, 2012, at A1; Kimberly Kindy et al., *Personal Interests, Bills Can Overlap*, WASH. POST, Oct. 8, 2012, at A1; Kimberly Kindy & Robert E. O'Harrow Jr., *The Dingells and GM Illustrate a Capitol Hill Quandary*, WASH. POST, Jan. 11, 2010, at A1; Robert O'Harrow Jr. et al., *Policy, Portfolios and the Investor Lawmaker*, WASH. POST, Nov. 23, 2009, at A1; Robert O'Harrow Jr. & Dan Keating, *When Public Duties and Private Investments Intersect*, WASH. POST, June 14, 2010, at A1. Some of these, as well as other, investment practices have been scrutinized in a controversial book. *See generally* PETER SCHWEIZER, THROW THEM ALL OUT: HOW POLITICIANS AND THEIR FRIENDS GET RICH OFF INSIDER STOCK TIPS, LAND DEALS, AND CRONYISM THAT WOULD SEND THE REST OF US TO PRISON (2011).

6. *See infra* note 242 and accompanying text.

volume of stock that lawmakers own in publicly traded companies, render this insulation more troubling than ever before.

Change is not only desirable but also possible. The recently enacted Stop Trading on Congressional Knowledge ("STOCK") Act amends the federal securities laws to reflect a basic fiduciary principle: that all federal officials, including members of Congress, owe duties of trust and confidence to the federal government and its citizens with respect to material nonpublic information obtained in connection with their government service.[7] The STOCK Act, which passed Congress with landslide votes of 96-3 in the Senate and 417-2 in the House,[8] owes its statutory life to the public outcry that was generated by a ***60 Minutes*** segment claiming that congressional insider trading was "perfectly legal."[9] Heightened media attention to the overlap between lawmakers' investments and their legislative activity,[10] coupled with the increased transparency stemming from the STOCK Act's requirements for the prompt reporting of securities transactions, could well ignite a comparable demand for financial conflict-of-interest reform. President Obama provided the opening salvo in his 2012 State of the Union Address when he called for new legislation that would reduce the "deficit of trust" between Washington, D.C. and the rest of the country by prohibiting "any elected official from owning stocks in industries they impact."[11]

This Article proceeds in four parts. Part I introduces the fiduciary duty of loyalty and briefly explains how it guards against self-interested decision making by a corporation's directors. Part II examines the strict statutory schemes that regulate financial conflicts of interest in the executive and judicial branches. These two parts share common themes, and it is hardly a coincidence that many fundamental insights pertaining to ethics regulation in the executive branch stem from a study performed more than fifty years ago by the Association of the Bar of the City of New York

---

7. Stop Trading on Congressional Knowledge ("STOCK") Act of 2012, Pub. L. No. 112–105, §§ 4(b), 9(b), 126 Stat. 291 (codified at 15 U.S.C. § 78u-1(g)–(h)). The STOCK Act further specifies that members of Congress and congressional employees owe a duty to Congress itself. *Id.* § 4(b).

8. *See infra* note 271 and accompanying text.

9. *See 60 Minutes: Congress: Trading Stock on Inside Information?* (CBS television broadcast Nov. 13, 2011), *available at* http://www.cbsnews.com/8301-18560_162-57323527/congress-trading-stock-on-inside-information/ ("For now, the practice is perfectly legal, but some say it's time for the law to change.").

10. *See infra* text accompanying notes 236–42 (discussing recent studies and investigative reports).

11. President Barack Obama, Address Before a Joint Session of Congress on the State of the Union, 2012 DAILY COMP. PRES. DOCS. 48 (Jan. 24, 2012), *available at* http://www.gpo.gov/fdsys/pkg/DCPD-201200048/pdf/DCPD-201200048.pdf; *see also infra* text accompanying note 272 (quoting the President's remarks on signing the STOCK Act).

("NYCBA")[12] under the direction of two persons now widely regarded as intellectual giants in the field of corporate law: American Law Institute President Emeritus Roswell Perkins, who supervised the ALI's Principles of Corporate Governance Project,[13] and the late Bayless Manning,[14] a former Dean of Stanford Law School, famous for his pioneering scholarship on legal capital.[15] In 1970, a successor committee published a follow-up study that focused on conflicts of interest and ethics standards in the legislative branch.[16]

Part III shifts the focus to the legislative branch and evaluates the very different set of ethics rules and norms that Congress has traditionally applied—and continues to apply—to the financial investments held by its members and employees. Part III then analyzes the rationales put forth by lawmakers to justify the view that their financial conflicts are best deterred through public disclosure of personal investments and the discipline of the electoral process. It also provides a contemporary snapshot of lawmakers as stock market investors.

---

12. *See generally* SPECIAL COMM. ON THE FED. CONFLICT OF INTEREST LAWS, ASS'N. OF THE BAR OF THE CITY OF N.Y., CONFLICT OF INTEREST AND FEDERAL SERVICE (1960) [hereinafter NYCBA 1960 REPORT].

13. Roswell Perkins served as the Chairman of the NYCBA Special Committee on the Federal Conflict of Laws. *See id.* at xii; *see also Federal Conflict of Interest Legislation: Hearings on H.R. 1900, H.R. 2156, H.R. 2157, H.R. 7556, and H.R. 10575 Before the Antitrust Subcomm. (Subcomm. No. 5) of the H. Comm. on the Judiciary*, 86th Cong. 383 (1960) (testimony of Roswell B. Perkins); Roswell B. Perkins, *The New Federal Conflict-of-Interest Law*, 76 HARV. L. REV. 1113, 1113 (1963).

14. Dean Manning served as Staff Director of the NYCBA's Special Committee on the Federal Conflict of Interest Laws and, in 1961, as a member of President Kennedy's Advisory Panel on Ethics and Conflicts of Interest in Government. *See* BAYLESS MANNING, FEDERAL CONFLICT OF INTEREST LAW vii (1964); Bayless Manning, *The Purity Potlatch: An Essay on Conflicts of Interest, American Government, and Moral Escalation*, 24 FED. B.J. 239, 239–40 (1964).

15. The NYCBA's 1960 Report limited its study to "the conflicts of interest problem of the executive branch of the federal government." NYCBA 1960 REPORT, *supra* note 12, at 12. That report, in turn, profoundly influenced the 1962 legislation that revised the federal conflicts of interest statutes (codified as amended at 18 U.S.C. §§ 201–18). *See Hearing on H.R. 8140 to Strengthen the Criminal Laws Relating to Bribery, Graft, and Conflicts of Interest Before the S. Comm. on the Judiciary*, 87th Cong. 8 (1962) (statement of Sen. Kenneth Keating) (observing that "Congress ha[d] been struggling with this subject, but . . . [was] given a great assist in 1960 by the work and report of a special committee of the [NYCBA]"). Dean Manning's treatise compares the former conflict-of-interest statutes to Congress's 1962 revisions. *See generally* MANNING, *supra* note 14.

16. *See* SPECIAL COMM. ON CONG. ETHICS, ASS'N. OF THE BAR OF THE CITY OF N.Y., CONGRESS AND THE PUBLIC TRUST, at x (1970) [hereinafter NYCBA 1970 REPORT]; *see also infra* text accompanying notes 275–84 (discussing the study's observations and recommendations).

Part IV proposes a long overdue solution to the agency problem associated with the personal investment practices of lawmakers. Drawing from the fiduciary principles that apply to corporate directors and government officials in the executive and judicial branches, it argues for new limitations on the securities that lawmakers may hold during their congressional service. Specifically, and as a starting place, it dusts off and advances an NYCBA recommendation from 1970: that Congress prohibit its members (and their staffs) from holding securities in companies substantially affected by the work of any congressional committee on which they hold membership. But given the ensuing changes in both legislative activity and stock ownership by lawmakers, Congress should also explore the adoption of even stricter anticonflict restraints such as a statute or rule that would, subject to some narrow exceptions, prohibit members of Congress and senior staff officials from owning any securities other than government securities or shares in diversified mutual funds. Although a provision of this sort was advanced in the Senate and voted down as an amendment to the STOCK Act, there are very compelling reasons to try again.

I. CORPORATE DIRECTORS AND THE DUTY OF LOYALTY

A duty of loyalty promotes the main purpose of fiduciary law: "to prohibit fiduciaries from misappropriating or misusing entrusted property or power."[17] Loyalty requires acting solely for the benefit of one's entrustor and never for any personal benefit. This sole-benefit edict is facilitated by a set of rules that prohibits certain actions outright "even though they are not necessarily injurious" to the entrustor.[18] These prophylactic rules serve "to dampen the fiduciaries' temptations to misappropriate entrusted property or power, or to justify benefitting themselves, and establish a continuous reminder that entrusted property and power do not belong to the fiduciaries."[19]

Rules that guard against self-interested decision making reflect two essential components of a fiduciary's duty of loyalty: a conflict component and an avoidance component.[20] The conflict component, as Professor Kathleen Clark explains, "prohibits a fiduciary from placing herself in a position where her own interest conflicts with her duty toward the beneficiary."[21] The avoidance component

---

17. FRANKEL, *supra* note 3, at 108.
18. *Id.*
19. *Id.*
20. *See* Clark, *supra* note 3, at 71 (drawing from the work of Robert Flannigan, *The Fiduciary Obligation*, 9 OXFORD J. LEGAL STUD. 285 (1989)).
21. *Id.*

"prohibits certain fiduciaries from delegating their duties to others or putting themselves in a position where, because of conflict or other concerns, they could not act on behalf of the beneficiary."[22]

Like fiduciary law more generally, corporate law has long been on guard against financial conflicts of interest that could compromise the duty of loyalty owed to a corporation by those who manage and direct its business. Indeed, the common law—at least at one time—allowed a corporation or its shareholders to void an "interested-director" transaction at will, regardless of the fairness or unfairness of the transaction.[23] Courts applying this blanket rule of voidability grounded it in the conflict component of a fiduciary obligation. As Justice Field observed in *Wardell v. Union Pacific Railroad Co.*:[24]

> It is among the rudiments of the law that the same person cannot act for himself and at the same time, with respect to the same matter, as the agent of another whose interests are conflicting. . . . Directors of corporations, and all persons who stand in a fiduciary relation to other parties, and are clothed with power to act for them, are subject to this rule; they are not permitted to occupy a position which will conflict with the interest of parties they represent and are bound to protect. They cannot, as agents or trustees, enter into or authorize contracts on behalf of those for whom they are appointed to act, and then personally participate in the benefits.[25]

Courts presented with financial conflicts that could taint director decision making were willing to presume harm to the corporation, even without any evidence to that effect, for a number of reasons. First, courts were highly skeptical that interested directors possessed the wherewithal to separate their own financial well-being from their corporate decision making. Moreover, courts assumed that in "a conflict between interest and duty . . . 'in the majority of cases duty would be overborne in the struggle.'"[26] Courts were also concerned about structural bias in the corporate boardroom—the very likely possibility that one or more directors with a conflict could exert subtle pressure on fellow directors. In this regard, courts questioned the ability of law "to accurately measure the influence of a trustee with his associates."[27]

---

22. *Id.*

23. *See generally* ROBERT CHARLES CLARK, CORPORATE LAW § 5.1 (1986); Harold Marsh, Jr., *Are Directors Trustees? Conflict of Interest and Corporate Morality*, 22 BUS. LAW. 35, 36 (1966).

24. 103 U.S. 651 (1880).

25. *Id.* at 658.

26. *Id.* (quoting Marsh v. Whitmore, 88 U.S. 178, 183–84 (1874)).

27. Munson v. Syracuse, 8 N.E. 355, 358 (N.Y. 1886).

Corporate law, however, rather quickly evolved to recognize the validity of interested-director transactions under certain sets of circumstances. The evolution began with courts placing a legal burden on the interested director to prove *both* that the transaction was entirely fair to the corporation (despite the presence of the conflict) *and* that the transaction had been approved by a fully informed and disinterested majority of board members.[28] This judicial development was fueled by practicality more than anything else.[29] Interested-director transactions were sometimes beneficial to the corporation, such as in instances where directors were willing to provide loans to corporations with dubious records of credit.[30] And certain interested-director transactions, such as compensation decisions for board members and officers, are impossible to avoid entirely.[31] The evolution continued when courts allowed directors to defend against breach of loyalty claims through a showing that an interested-director transaction was entirely fair to the corporation whether or not that transaction had been approved by a disinterested majority of the board.[32]

Today, statutory provisions in the corporate law of every state have built on these judicial developments by specifying alternative mechanisms pursuant to which an interested-director transaction can be "sanitized." Section 144(a) of the Delaware General Corporation Law,[33] for example, specifies three distinct ways by which an interested-director transaction can survive a litigation challenge: (1) approval in good faith, after full disclosure, by a majority of disinterested directors; (2) approval in good faith, after full disclosure, by a majority of disinterested shareholders; or (3) proof that the transaction was entirely fair to the corporation.[34] The Model Business Corporation Act ("MBCA") has similar provisions on "Directors' Conflicting Interest Transactions."[35] Thus, under these

---

28. *See* CLARK, *supra* note 23, at 160.

29. *See* STEPHEN A. BAINBRIDGE, CORPORATION LAW AND ECONOMICS 308 (2002) (emphasizing practicality, but also recognizing that a per se rule of voidability "fails to give due deference to the principles of party autonomy and freedom of contract, which are important values both in themselves and because they promote efficient transactions").

30. *See* CLARK, *supra* note 23, at 185.

31. Claire Hill & Brett McDonnell, *Sanitizing Interested Transactions*, 36 DEL. J. CORP. L. 903, 909 (2011).

32. Marsh, *supra* note 23, at 43–44 (observing that from 1910 to 1960, there were a large number of cases which dealt with situations "where a majority of the board w[as] interested and which discuss them solely in terms of a review of the fairness of the transaction, without bothering to cite or discuss any of the previous decisions . . . enunciating the rule that there must be approval by a disinterested majority of the board").

33. DEL. CODE ANN. tit. 8, § 144 (2011).

34. *Id.* § 144(a)(1)–(3).

35. MODEL BUS. CORP. ACT §§ 8.60–.63 (2005).

statutory provisions, interested-director transactions can be valid and enforceable as long as they are *either* approved *or* fair. But because proving "entire fairness" to a court is both time consuming and expensive, boards typically take advance steps to ensure that interested directors make full disclosure about their conflicts and then recuse themselves from any decision to approve the transaction.[36]

What is most important, given this Article's focus on lawmakers, is that in Delaware and every other state, interested-director transactions stand out as a fundamental exception to the business judgment rule that would otherwise apply to decisions made by corporate boards. The business judgment rule reflects a basic presumption that when directors make a decision, they do so "on an informed basis, in good faith, and in the honest belief that the action was taken in the best interests of the corporation."[37] The rule thus serves to insulate most board decisions from litigation challenges by shareholders as well as second-guessing by courts. However, courts will not apply the business judgment rule—that is, courts will not automatically presume good faith and loyal decision making on the part of directors—if shareholders can offer evidence that one or more board members stood to gain personally from a corporate transaction.[38]

Because courts will not presume that directors will necessarily resolve all conflicts in accordance with the corporation's best interests, interested-director transactions trigger the need for judicial review. When such a transaction has been approved by a majority of disinterested directors or shareholders, the extent of judicial scrutiny is minimal.[39] The scrutiny centers on the nature of the process for approval, with the central focus on whether all relevant facts pertaining to the conflict were fully disclosed and whether the directors (or shareholders) who approved the transaction were in fact disinterested and acting in good faith.[40] If a court determines that the processes for director approval or shareholder approval were satisfactory, the protection of the business judgment rule is effectively restored, and litigation will typically be dismissed unless another reason, independent of the

36. *See generally* Hill & McDonnell, *supra* note 31.

37. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

38. *See* Weinberger v. UOP, Inc., 457 A.2d 701, 710 (Del. 1983) ("When directors of a Delaware corporation are on both sides of a transaction, they are required to demonstrate their utmost good faith . . . .").

39. Hill & McDonnell, *supra* note 31, at 914.

40. *Id.* at 913–14.

conflict, exists for challenging the transaction.[41] In contrast, interested-director transactions that have not been sanitized by disinterested decision makers trigger a much higher degree of judicial scrutiny. Under the "entire fairness" test, courts will insist that the defendants bear the burden of proving that the challenged transaction was concluded at a fair price and involved fair dealing.[42] Fair dealing "embraces questions of when the transaction was timed, how it was initiated, structured, negotiated, disclosed to the directors, and how the approvals of the directors and the stockholders were obtained."[43] A director's failure to disclose a conflict of interest is generally regarded as compelling evidence of unfair dealing.[44]

Whether judicial scrutiny is minimal pursuant to a process-based safe harbor or rigorous under an entire fairness test, modern corporate law continues to view the possibility of personal gain from corporate transactions with suspicion. To be sure, the common law rule of automatic voidability has been replaced with statutory provisions that are far more tolerant of conflicts. But Delaware section 144 and the like simply reflect a legislative judgment that a corporation's disinterested directors or shareholders, after full disclosure of a conflict, constitute effective "reviewers."[45] The need for impartial review in conflict-of-interest situations has never been questioned. Nor has there been a retreat from the loyalty-based rule that corporate directors must act solely for the benefit of the corporation and not for their own personal benefit.

II. FINANCIAL CONFLICTS AND FEDERAL OFFICIALS OUTSIDE OF CONGRESS

The design and structure of our federal government draws from the very same fiduciary principles that underlie corporate law. Federal officials—whether elected or appointed—are entrusted with political power, and they are thus expected to place the public's best interest ahead of their own self-interest. Indeed, as others have

41. *See* Benihana of Tokyo, Inc. v. Benihana, Inc., 906 A.2d 114, 120 (Del. 2006) (stating that "[a]fter approval by disinterested directors, courts review the interested transaction under the business judgment rule").

42. *Weinberger*, 457 A.2d at 711.

43. *Id.*

44. *See generally* MODEL BUS. CORP. ACT § 8.60, cmt. 6(b) (2005) (observing that "[o]ne illustration of unfair dealing is the director's failure to disclose fully the director's interest . . . regarding the transaction"); *see also* HMG/Courtland Props., Inc. v. Gray, 749 A.2d 94, 116 (Del. Ch. 1999) (ruling that process was "anything but fair" when one director knew of another director's interest in the transaction, but neither disclosed that interest to their fellow directors).

45. *See* Hill & McDonnell, *supra* note 31, at 921.

emphasized,[46] the U.S. Constitution refers in multiple places to "public Trust"[47] and to public offices being "of Trust."[48] The Constitution also includes several provisions expressly designed to guard against self-interested decision making.[49] Anticonflict measures were much on the minds of the framers because, as James Madison explained in *The Federalist*:

> The aim of every political constitution is, or ought to be, first to obtain for rulers men who possess most wisdom to discern, and most virtue to pursue, the common good of the society; and in the next place, to take the most effectual precautions for keeping them virtuous whilst they continue to hold their public trust.[50]

Congress built on this constitutional conception of a public office as a public trust across a wide range of federal ethics statutes, which employ a variety of mechanisms for keeping government officials "virtuous" (thereby, in corporate parlance, mitigating agency costs). Criminal anticorruption statutes, such as those that prohibit the receipt of bribes[51] and illegal gratuities,[52] are obvious examples.[53] Other criminal statutes, often described generally as "conflicts of interest statutes,"[54] regulate such matters as a federal official's acceptance of gifts[55] or the receipt of outside earned income,[56] or they prohibit the representation of third parties before

---

46. FRANKEL, *supra* note 3, at 282 (quoting Natelson, *supra* note 3, at 1086).

47. U.S. CONST. art. VI, cl. 3.

48. *Id.* art. I, § 3, cl. 7; *id.* art. I, § 9, cl. 8; *id.* art. II, § 1, cl. 2.

49. *See, e.g.*, *id.* art. I, § 9, cl. 8 ("[N]o Person holding any Office of Profit or Trust under [the United States] shall, without the Consent of the Congress, accept any present, Emolument, Office, or Title, of any kind whatever, from any King, Prince, or foreign State."); *id.* art. I, § 6, cl. 2 (prohibiting members of Congress from being appointed to a federal office that was created or that received an increase in salary during their time in Congress); *id.* amend. XXVII (prohibiting a member of Congress from receiving an increase in salary until after he/she stands for reelection); *see also* Daniel L. Koffsky, *Coming to Terms with Bureaucratic Ethics,* 11 J. L. & POL. 235, 238–43 (1995) (discussing conflict-of-interest restrictions in the Constitution).

50. THE FEDERALIST NO. 57, at 327 (James Madison).

51. 18 U.S.C. § 201(b)(1)(a) (2006) (making it a crime for both the offeror and the public official to corruptly engage in a transfer of anything of value with the intent to influence any official act).

52. *Id.* § 201(c) (making it a crime to provide (or accept) a gratuity "for or because of" the official's performance of an official act "otherwise than as provided by law for the proper discharge of official duty").

53. For others, see generally PETER J. HENNING & LEE J. RADEK, THE PROSECUTION AND DEFENSE OF PUBLIC CORRUPTION (2011).

54. *See* NYCBA 1960 REPORT, *supra* note 12, at ch. III.

55. 5 U.S.C. § 7353 (2006).

56. 18 U.S.C. § 209.

government agencies.[57] Financial reporting statutes, which have their origins in the fiduciary obligation of disclosure, constitute another important example.[58]

The Ethics in Government Act of 1978 ("EIGA")[59] provides the statutory basis for the financial reporting duties of federal officials in all three branches of the government. Designed in large part to reveal and deter financial conflicts of interest, the EIGA requires hundreds of thousands of federal officials to file annual statements that disclose their income (other than earned income from U.S. government employment), financial holdings (asset values may be specified in certain dollar ranges in lieu of exact amounts), gifts, travel reimbursements, liabilities, and business affiliations.[60] Although low-level government employees are generally entitled to file their disclosure forms confidentially, the public has access (by request) to the financial disclosure statements submitted by thousands of other "public filers."[61] Recent STOCK Act amendments to the EIGA promote even greater transparency and accountability by requiring the President, Vice President, any member of Congress, any candidate for Congress, and certain presidentially appointed, Senate-confirmed executive branch officials to promptly supplement their annual forms by reporting most new financial transactions over $1,000 no later than forty-five days after the purchase or sale (diversified mutual fund transactions are not covered).[62] These reports shall be made available to the public on official House and Senate websites for the legislative branch and on the Office of Government Ethics website for the

57. *Id.* § 203.

58. *See, e.g.*, Ethics in Government Act of 1978, Pub. L. No. 95-521, 92 Stat. 1824 (codified as amended in scattered §§ of 2, 5, 18 and 28 U.S.C.).

59. *Id.*

60. 5 U.S.C. app. §§ 101–02.

61. *See* Kathleen Clark, *Ethics, Employees and Contractors: Financial Conflicts of Interest in and out of Government*, 62 ALA. L. REV. 961, 970 (2011) (observing that each year, the executive branch alone has approximately 25,000 employees who submit public disclosure forms and 300,000 additional employees who submit confidential disclosure forms). In addition to members of Congress, "public filers" in the legislative branch include "senior staff," a term used to denote an officer or employee whose annual base salary exceeds a specified level. *See* JACK MASKELL, CONG. RESEARCH SERV., R42495, THE STOCK ACT, INSIDER TRADING, AND PUBLIC FINANCIAL REPORTING BY FEDERAL OFFICIALS 3 (2013), *available at* http://www.fas.org/sgp/crs/misc/R42495.pdf. Officers and employees earning an annual salary of approximately $120,000 or above were considered senior staff when the STOCK Act became law. *See* 158 CONG. REC. S243 (Feb. 1, 2012) (statement by Sen. Sherrod Brown).

62. STOCK Act, Pub. L. No. 112–105, § 6(a), 126 Stat. 291, 293–94 (2012) (codified at 5 U.S.C. app. § 103).

executive branch.[63] Although their financial transaction reports will not be available online, all other public filers in the legislative and executive branches under the EIGA are required to adhere to the STOCK Act's provisions for prompt reporting of personal financial transactions.[64]

In addition to the EIGA's disclosure requirements, federal officials in the executive and judicial branches are governed by a strict statutory framework that expressly prohibits these officials from participating or rendering decisions in matters that affect their own financial interests.[65] Financial disclosure requirements thus facilitate the investigation and enforcement of financial conflict-of-interest laws. But, as we shall see in Part III, legislative branch officials generally function free from explicit, financial conflict-of-interest restraints.[66] Instead, Congress presumes that a lawmaker is generally able to decide for him or herself what the duty of loyalty requires. Public financial disclosures under the EIGA and electoral accountability are thus the principal means of monitoring and deterring financial conflicts of interest on the part of lawmakers and most congressional employees.

A. *Executive Branch Officials*

Financial conflicts of interest that could possibly bias an executive branch official's decision making are addressed most directly in 18 U.S.C. § 208, a broadly worded statute entitled "Acts Affecting a Personal Financial Interest." Its basic precept, in the words of the NYCBA's 1960 Report, is that a public official "should not act for the government where his private economic interests are involved."[67] Section 208 subjects to imprisonment or other penalties any "officer or employee of the Executive branch of the United States Government, or of any independent agency of the United States" who

> participates personally and substantially as a Government officer or employee, through decision, approval, disapproval, recommendation, the rendering of advice, investigation, or

---

63. *Id.* §§ 8(b), 11(b). *But see* Pub. L. No. 113-7, § 1, 127 Stat. 438, 438–39 (2013) (adjusting the STOCK Act's online availability date to January 14, 2014 and rescinding the previous requirement that these databases be maintained in a manner allowing the public to "search, sort and download data contained in the reports").

64. § 6(a), 126 Stat. at 293; § 1(a), 127 Stat. at 438 (permanently rescinding the STOCK Act's previous requirement for Internet posting of transaction reports for most public filers in the legislative and executive branches of the government).

65. *See infra* Subparts II.A, II.B.

66. *See infra* Part III.

67. *See* NYCBA 1960 REPORT, *supra* note 12, at 198.

> otherwise, in a judicial or other proceeding, application, request for a ruling or other determination, contract, claim, controversy, charge, accusation, arrest, or other particular matter in which, to his knowledge, he, his spouse, minor child, general partner, organization in which he is serving as officer, director, trustee, general partner or employee, or any person or organization with whom he is negotiating or has any arrangement concerning prospective employment, has a financial interest . . . .[68]

Although there is some disagreement as to whether the Constitution allows § 208's prohibition to reach the President and Vice President, government ethics scholars observe that the issue is not likely to be tested, "because presidents and vice presidents already conscientiously seek to comply with the conflicts of interest statutes regardless of whether the statutes apply."[69]

By criminalizing the mere possibility of actions involving divided loyalty on the part of executive branch officials, Congress ensured that these decision makers would take seriously the conflict component of their fiduciary obligation.[70] Officials in the executive branch have two clear alternatives: either recuse or divest whenever one's participation in a "particular matter" could implicate one's own financial self-interest, unless an exemption is available.[71] As the Supreme Court emphasized in *United States v. Mississippi Valley Generating Co.*[72]:

> The statute is directed at an evil which endangers the very fabric of a democratic society, for a democracy is effective only if the people have faith in those who govern, and that faith is bound to be shattered when high officials and their appointees engage in activities which arouse suspicions of malfeasance and corruption. The seriousness of this evil quite naturally led

---

68. 18 U.S.C. § 208(a) (2006).
69. *See* PAINTER, *supra* note 3, at 59–61.
70. *See supra* text accompanying note 21.
71. Section 208 contains four principal exemptions: (1) if the official makes full disclosure of the financial interest and seeks an advance waiver from the agency head, who determines that the "interest is not so substantial as to be deemed likely to affect the integrity of the services which the Government may expect from such officer or employee;" (2) if the Office of Government Ethics has issued a regulation exempting the financial interest from the statute's application because it is "too remote or too inconsequential" to affect the integrity of government services; (3) if the official is serving in a temporary position on a federal advisory committee and a senior official opts to waive the conflict based on the need for that official's services; (4) if the financial interest involves a claim of a Native American birthright. 18 U.S.C. § 208(b).
72. 364 U.S. 520 (1961).

Congress to adopt a statute whose breadth would be sufficient to cope with the evil.[73]

Because it is aimed at executive branch decisions that simply "arouse suspicion," § 208 employs an objective standard for liability and requires no showing of actual corruption or bad faith intent. Courts have held that the statute's "to his knowledge" modifier applies only to the official's "financial interest" and not to the crime itself.[74] Thus, as long as an executive branch official is aware of a financial holding covered by the statute, even an official's good faith participation in an agency matter can be subject to criminal prosecution.[75] Chief Justice Earl Warren highlighted this objective standard when he observed that the statute is "directed not only at dishonor, but also at conduct that tempts dishonor. . . . [It] is more concerned with what might have happened in a given situation than with what actually happened."[76]

Congress directed the U.S. Office of Government Ethics ("OGE") to interpret the statute and promulgate certain exemptions in executive branch-wide regulations.[77] Pursuant to that authority, the OGE has construed the term "particular matter" to include "[any] judicial or other proceeding, application, request for a ruling or other determination, contract, claim, controversy, investigation, charge, accusation or arrest" as well as "matters which do not involve formal parties . . . [such as] legislation or policy making that is narrowly focused on the interests of a discrete and identifiable class of persons."[78] Thus, a particular matter could include a Department of Agriculture regulation directed at companies that operate meat packing plants,[79] or a prescription drug regulation by the Food and Drug Administration ("FDA") applicable to pharmaceutical companies.[80] But it would not include Department of Labor changes to health and safety regulations pertaining to all

73. *Id.* at 562 (referencing 18 U.S.C. § 434, the financial conflict statute that was the statutory predecessor to 18 U.S.C. § 208); *accord* United States v. Gorman, 807 F.2d 1299, 1304 n.1 (6th Cir. 1986) (observing that *Mississippi Valley* "remains applicable" because "the purpose of Section 208 is to strengthen its predecessor without changing any of its underlying policies") (internal quotes omitted).

74. *See, e.g.*, United States v. Hedges, 912 F.2d 1397, 1401 (11th Cir. 1990).

75. *See* David R. Flickinger, *Attracting the Best and the Brightest to Government Service: Requiring Scienter for Criminal Conflicts of Interest*, 25 GEO. J. LEGAL ETHICS 519, 520 (2012) (acknowledging the objective standard of liability under prevailing precedents, but arguing that courts should instead impose a requirement of criminal intent).

76. *Miss. Valley*, 364 U.S. at 549–50.

77. 18 U.S.C. § 208(d)(2).

78. 5 C.F.R. § 2640.103(a)(1) (2012).

79. *Id.* ex. 3.

80. *Id.* ex. 8.

U.S. employers, because such a change would affect virtually every publicly traded corporation in the nation, and thus it would be directed "to the interests of a large and diverse group of persons."[81]

The OGE has also clarified that the statutory proscription applies only if the particular matter would have a "direct and predictable effect" on the participating employee's financial interest.[82] "Direct" is defined as "a close causal link between any decision or action to be taken in the matter and any expected effect of the matter on the financial interest"[83] and "predictable" is defined as "a real, as opposed to a speculative, possibility that the matter will affect the financial interest."[84] The regulations specifically contemplate that a "disqualifying financial interest might arise from ownership of certain financial instruments or investments, such as stock, bonds, mutual funds, or real estate."[85] Certain securities held in qualified blind trusts, however, are not considered "financial interests."[86] The OGE has also exempted holdings in diversified mutual funds and employee benefit plans as well as certain de minimis interests in publicly traded securities provided the market value of all personal holdings in the securities issuer does not exceed $15,000.[87]

The following scenario, included in OGE regulations, is illustrative of § 208's broad scope:

> An employee is assigned to monitor XYZ Corporation's performance of a contract to provide computer maintenance services at the employee's agency. At the time the employee is first assigned these duties, he owns publicly traded stock in XYZ Corporation valued at less than $15,000. During the time the contract is being performed, however, the value of the employee's stock increases to $17,500. When the employee knows that the value of his stock exceeds $15,000, he must disqualify himself from any further participation in matters affecting XYZ Corporation or seek an individual waiver under 18 U.S.C. 208(b)(1). Alternatively, the employee may divest the portion of his XYZ stock that exceeds $15,000. This can be accomplished through a standing order with his broker to sell when the value of the stock exceeds $15,000.[88]

---

81. *Id.* ex. 4.
82. *Id.* § 2640.103(a)(3).
83. *Id.* § 2640.103(a)(3)(i).
84. *Id.* § 2640.103(a)(3)(ii).
85. *Id.* § 2640.103(b).
86. *Id.* § 2634.401(a).
87. *Id.* § 2640.201. The OGE's de minimis exception, however, serves as the default rule. Individual agencies may enact regulations specifying lower thresholds for its employees or eliminating the exception entirely.
88. *Id.* § 2640.202(a) ex. 3.

The example demonstrates that § 208 criminalizes the employee's participation in an XYZ matter even if his $2,500 in stock holdings above the de minimis amount was exceedingly unlikely to influence his monitoring of XYZ's computer services contract. When a violation of § 208 is discovered (whether through a supervisor's review of an official's financial disclosure filings or otherwise), the agency that employs that official will typically coordinate with its office of Inspector General to ensure that the matter is referred to the Public Integrity Section of the Department of Justice, which ultimately determines whether a prosecution is warranted.[89]

Congress has likewise enacted legislation that reflects the avoidance component of an executive branch official's fiduciary obligation.[90] Although there is not a single government-wide statute that requires an executive branch official to divest financial interests in circumstances where a § 208-prompted recusal would fundamentally interfere with his or her government responsibilities,[91] there is a host of agency-specific statutes that prohibit officials from holding financial interests in certain entities. For example, the first Congress prohibited the Secretary of the Treasury and the Treasurer from investing in securities issued by the federal government or the states.[92] Statutory prohibitions may also apply agency wide: Federal Communications Commission ("FCC") employees, for instance, are prohibited from holding financial interests in any company engaged in radio or wire communication.[93] Particular congressional committees, often as a condition of Senate confirmation, may likewise restrict the financial holdings of certain executive branch officials. The Senate Armed Services Committee, for instance, prohibits presidential appointees to positions in the Department of Defense ("DOD") from owning stocks or bonds in the nearly 50,000 companies that have contracts with the Pentagon.[94] Notably, Congress has amended the tax code to allow for the deferral of capital gains tax when a federal official sells assets to avoid conflicts of interest.[95]

The avoidance component of an executive branch official's fiduciary obligation is further reflected in certain agency-specific

---

89. *See Enforcement*, U.S. OFF. GOV'T ETHICS, http://www.oge.gov/Topics/Enforcement/Enforcement/ (last visited July 16, 2013).

90. *See* Clark, *supra* note 3, at 90.

91. *See id.*

92. *See* Donna M. Nagy & Richard W. Painter, *Selective Disclosure by Federal Officials and the Case for an FGD (Fairer Government Disclosure) Regime*, 2012 WIS. L. REV. 1285, 1297–98 & n.56 (discussing the insider trading scandal that prompted this statutory prohibition).

93. 47 U.S.C. § 154(b)(2)(A)(ii) (2006).

94. *See* Higham et al., *supra* note 5.

95. *See* PAINTER, *supra* note 3, at 42.

regulations. That is, individual agencies have broad authority to issue regulations prohibiting all or some employees from specific categories of financial investments "based on the agency's determination that the acquisition or holding of such financial interest would cause a reasonable person to question the impartiality and objectivity with which agency programs are administered."[96] The FDA, for example, prohibits most of its employees from holding any financial interest in a "significantly regulated organization."[97] Moreover, agencies may prohibit an individual employee from holding or acquiring financial interests that will "[r]equire the employee's disqualification from matters so central or critical to the performance of his official duties that the employee's ability to perform the duties of his position would be materially impaired,"[98] or "adversely affect the efficient accomplishment of the agency's mission because another employee cannot be readily assigned."[99]

Whether the "interest avoidance" is imposed by federal statute or by an administrative regulation, and whether it applies to a particular person or to persons across an entire agency, its objective is the same: to eliminate financial interests that could possibly tempt an executive branch official into subordinating the public interest to his or her own self-interest.[100] Consistent with the fiduciary principle, the protection of the integrity of government decision making is paramount.[101]

B. *Judicial Branch Officials*

The primary judicial recusal statute, 28 U.S.C. § 455, embodies the conflict component of a fiduciary obligation. Pursuant to this statute, any U.S. justice, judge, or magistrate judge is required to disqualify himself or herself in any proceeding in which his or her "impartiality might be reasonably questioned."[102] The statute further mandates recusal in any one of five specific circumstances. These circumstances include a judge's financial interest, when such an official

96. 5 C.F.R. § 2635.403(a) (2012).

97. *Id.* § 5501.104. An organization is "significantly regulated" if the sales of products regulated by the FDA would "constitute ten percent or more of annual gross sales in the organization's previous fiscal year." *Id.* § 5501.104(c)(2).

98. *Id.* § 2635.403(b)(1).

99. *Id.* § 2635.403(b)(2).

100. *See* NYCBA 1970 REPORT, *supra* note 16, at 40–41.

101. *Id.* at 41.

102. 28 U.S.C. § 455(a) (2006). *See generally* Charles Gardner Geyh, *Judicial Disqualification: An Analysis of Federal Law*, FED. JUD. CENTER, http://www.fjc.gov/public/pdf.nsf/lookup/judicialdq.pdf/$file/judicialdq.pdf (last visited Sept. 4, 2013).

> knows that he, individually or as a fiduciary, or his spouse or minor child residing in his household, has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding.[103]

"Financial interest" is defined broadly to mean "ownership of a legal or equitable interest, however small, or a relationship as director, advisor or other active participant in the affairs of a party."[104] But the term specifically excludes "[o]wnership in a mutual or common investment fund that holds securities . . . unless the judge participates in the management of the fund"[105] as well as "[o]wnership of government securities . . . [unless] the outcome of the proceeding could substantially affect the value of the securities."[106] The statute also makes clear that judges have a duty to inform themselves about their personal financial interests and the financial interests of their spouses and minor children residing in their household.[107]

The judicial recusal statute's reference to financial ownership interests "however small" forecloses any de minimis exception. State court judges typically operate under judicial codes that define financial interests to mean "more than a de minimis interest,"[108] and as we have seen, OGE regulations include de minimis exceptions in connection with publicly traded securities held by officials in the executive branch.[109] But § 455 imposes "a bright line rule [that] requires recusal based on ownership of even a single share of stock in a party"[110] or in a company substantially affected by the subject matter in controversy.[111] It also states explicitly that a judge's disqualification for a financial interest is not subject to waiver by the parties.[112]

Section 455 does, however, provide a limited mechanism by which judges may divest themselves of certain financial interests that would otherwise disqualify them from presiding over a proceeding. The relevant provision specifies that

> [n]otwithstanding the preceding provisions of this section, if any justice, judge, magistrate judge, or bankruptcy judge to

103. 8 U.S.C. § 455(b)(4) (2006).
104. *Id.* § 455(d)(4).
105. *Id.* § 455(d)(4)(i).
106. *Id.* § 455(d)(4)(iv).
107. *Id.* § 455(c).
108. M. Margaret McKeown, *To Judge or Not to Judge: Transparency and Recusal in the Federal System*, 30 REV. LITIG. 653, 662–63 (2011).
109. *See supra* note 87 and accompanying text.
110. McKeown, *supra* note 108, at 662–63 n.57.
111. *Id.*
112. 28 U.S.C. § 455(e) (2006).

> whom a matter has been assigned would be disqualified, after substantial judicial time has been devoted to the matter, because of the appearance or discovery, after the matter was assigned to him or her, that he or she individually or as a fiduciary, or his or her spouse or minor child residing in his or her household, has a financial interest in a party (other than an interest that could be substantially affected by the outcome), disqualification is not required if the justice, judge, magistrate judge, bankruptcy judge, spouse or minor child, as the case may be, divests himself or himself of the interest that provides the grounds for the disqualification.[113]

Thus, a judge may avert the need for recusal—through divestiture—if she does not discover the financial interest until after she has devoted significant time to the matter and if the financial interest at issue could not be substantially affected by the matter's outcome.

Congress enacted § 455 to ensure that judges assess for themselves whether a conflict of interest requires them to decline an assignment or to recuse themselves from a case that has already been assigned.[114] The judiciary has also implemented institutional safeguards to avoid financial conflicts, such as the random drawing of assignments as well as an electronic conflicts screening system that flags a judge's previously reported financial interests that could trigger the need for disqualification.[115] But in the absence of a judge's voluntary withdrawal, § 455 permits parties to move for recusal. Moreover, judges who fail to recuse themselves when circumstances warrant may be subject to a judicial conduct complaint initiated by a litigant, a member of the public, or the chief judge of the circuit.[116] In particularly egregious cases, judges could be impeached.[117]

---

113. *Id.* § 455(f). Notably, § 455(c)'s due diligence requirement for personal and family member investments, *see supra* text accompanying note 107, substantially reduces the likelihood of a "discovery" that would trigger this divestiture alternative.

114. McKeown, *supra* note 108, at 664.

115. *Id.*

116. *Id.* at 665 (citing *Judicial Conduct & Disability Act: Resources*, U.S. CTS., http://www.uscourts.gov/RulesAndPolicies/ConductAndDisability/JudicialConductDisability.aspx (last visited Sept. 4, 2013) (giving the codes of conduct in each circuit)). The disqualification requirements set out in 28 U.S.C. § 455 are transcribed virtually verbatim into Canon 3C of the Code of Conduct for U.S. Judges. *See Guide to Judiciary Policy*, U.S. CTS., http://www.uscourts.gov/uscourts/RulesandPolicies/conduct/Vol02A-Ch02.pdf.

117. *See* Geyh, *supra* note 102, at 27 (observing that Judge G. Thomas Porteous, Jr. from the Eastern District of Louisiana was impeached, found guilty by the Senate, and removed from office in 2010 based on his refusal to disqualify himself from hearing a case in which a party was represented by a lawyer from whom he had recently solicited—and years before received—money to pay personal gambling and other debts).

III. Financial Conflicts and the Legislative Branch

Like corporate directors and federal officials in the executive and judicial branches, members of Congress and their staffs serve as agents with fiduciary obligations to their principals. But while few would dispute that congressional officials owe a duty of loyalty to the federal government and the public, the prophylactic rules that guard against financial conflicts in corporations and in the other two branches of government have been regarded as unwarranted in the legislative branch. After addressing the principal rationales offered by lawmakers in defense of the status quo and examining some facts about lawmakers as stock market investors, this Part draws a very different conclusion.

A. *Lawmakers as Fiduciaries*

In both the U.S. Senate and the House of Representatives, rules and other official pronouncements proudly decree that a "public office is a public trust."[118] But as Jack Maskell emphasized in congressional hearings on the STOCK Act, this phrase is "more than merely an aphorism, because it denotes that Members of Congress who wield public power have a fiduciary responsibility to use that power in the interests of the general public who are supposed to be the beneficiaries of that trust."[119] The STOCK Act itself was premised on an existing fiduciary obligation of loyalty,[120] and that premise is now embodied in the Act's explicit dictate that all federal officials, including members of Congress, owe a duty "arising from a relationship of trust and confidence" to the federal government and its citizens with respect to material, nonpublic information obtained in connection with their government service.[121] Congressional

118. Code of Ethics for Government Service, H.R. Con. Res. 175, 85th Cong. ¶ 10 (1958); STAFF OF S. SELECT COMM. ON ETHICS, 108TH CONG., SENATE ETHICS MANUAL at 11, 21, 184, 436 (Comm. Print 2003) [hereinafter SENATE ETHICS MANUAL], *available at* http://ethics.senate.gov/downloads/pdffiles/manual.pdf; H. COMM. ON STANDARDS OF OFFICIAL CONDUCT, 110TH CONG., HOUSE ETHICS MANUAL 2, 23, 151, 187, 215, 355 (2008) [hereinafter HOUSE ETHICS MANUAL], *available at* http://ethics.house.gov/sites/ethics.house.gov/files/documents/2008_House_Ethics_Manual.pdf.

119. *The Stop Trading on Congressional Knowledge Act: Hearing on H.R 1148 Before the H. Comm. on Fin. Servs.*, 112th Cong. 83–84 (2011) [hereinafter *House STOCK Act Hearing*] (written statement by Jack Maskell, Legislative Attorney, American Law Division, Congressional Research Service).

120. *See* 158 CONG. REC. S1977–78 (daily ed. Mar. 22, 2012) (statement of Sen. Susan Collins) (describing "the affirmation of a duty arising from the relationship of trust and confidence" as the "heart" of the Act, and emphasizing that "this is not a new fiduciary duty, in the traditional sense, but the recognition of an existing duty").

121. STOCK Act, Pub. L. No. 112–105, § 4(b), 126 Stat. 291 (2012) (codified at 15 U.S.C. § 78u-1(g)–(h)).

fiduciary obligations also have a strong constitutional underpinning, as we have already seen.[122]

The fiduciary duty of members of Congress toward the public manifests itself in a host of other federal statutes apart from the STOCK Act's insider trading provisions and the EIGA's financial reporting requirements.[123] Some of these statutes, such as the conflict-of-interest statutes and the anticorruption statutes discussed previously, are tailored specifically toward conduct by lawmakers as a specific class or as part of a broader class of public officials.[124] Congress, for example, subjects its members and employees to strict statutory limitations on the gifts that they can receive, the honoraria that they can be paid for speaking engagements, and the work-related contacts they may have with their former colleagues in the two-year period following their departure from service in Congress.[125] Other federal statutes have broader application but can be used by prosecutors to charge official misconduct, such as the mail fraud[126] and wire fraud statutes,[127] which can encompass congressional breaches of loyalty in cases involving bribes and kickbacks (often referred to as "honest services fraud")[128] as well as the misappropriation of property.[129]

---

122. *See supra* notes 47–50 and accompanying text. *See also* Natelson, *supra* note 3, at 1083–84 (observing that at the time of the federal constitutional convention, "most of the state constitutions already contained fiduciary language" and that during the public debate over the Constitution, "leading proponents of the new government repeatedly characterized officials as the people's servants, agents, guardians, or trustees"); Rave, *supra* note 3, at 708–13 (discussing constitutional history and political theory).

123. *See supra* notes 59–64 and accompanying text.

124. *See supra* notes 51–57 and accompanying text.

125. *See* PAINTER, *supra* note 3, at 146–52.

126. 18 U.S.C. § 1341 (2006) (prohibiting "schemes or artifices to defraud" through use of the mails).

127. *Id.* § 1343 (prohibiting "schemes or artifices to defraud" through use of electronic wires, radio, or television).

128. *See Restoring Key Tools to Combat Fraud and Corruption After the Supreme Court's Skilling Decision: Hearing Before the S. Comm. on the Judiciary*, 111th Cong. 33 (2010) (written statement by Lanny A. Breuer, Assistant Attorney General, Criminal Division, Department of Justice) (stating that for decades, federal prosecutors have used the mail and wire fraud statutes to reach "schemes designed to deprive citizens of the honest services of public and private officials who owe them a fiduciary duty of loyalty"); *see also* Donna M. Nagy, *Insider Trading, Congressional Officials, and Duties of Entrustment,* 91 B.U. L. REV. 1105, 1145–50 (2011) (discussing honest service fraud prosecutions involving several former Members of Congress, including Representatives William Jefferson, Randy Cunningham, Richard Renzi, and Robert Ney).

129. *See* Nagy, *supra* note 128, at 1149–50 (discussing mail fraud convictions involving former Representatives Charles Diggs and Dan Rostenkowski).

In addition to federal statutes, the fiduciary duty of lawmakers to the public is reflected in ethics rules adopted and enforced by the Senate and the House Ethics Committee, respectively, and in the commentary set out in each chamber's Ethics Manual.[130] As the Constitution provides, congressional self discipline for "disorderly behavior" is administered by the member's own chamber.[131] And as the Supreme Court recognized in *In re Chapman*,[132] even the right to expel "extends to all cases where the offense is such as in the judgment of the [chamber] is inconsistent with the trust and duty of a member."[133]

Congress's own perception of lawmakers as fiduciaries is shared by federal courts, including the Supreme Court, as the above quotation from *Chapman* reflects. The Court implicitly avowed a congressional duty of loyalty in *Skilling v. United States*[134] when it observed that "[t]he existence of a fiduciary relationship . . . was beyond dispute" in several prior precedents, including a D.C. Circuit decision that had affirmed a former congressman's conviction for mail fraud.[135] In *United States v. Diggs*,[136] the court stated explicitly that the congressman's conduct "amounted to no less than a scheme to take illicit kick-backs" and that this scheme "defrauded the public of not only substantial sums of money but of his faithful and honest services."[137] The Second Circuit also applied a fiduciary theory in *United States v. Podell*,[138] a decision which affirmed a grant of summary judgment to the government for "monies [the defendant] had received in breach of his fiduciary duty as a United

---

130. *See also* HOUSE ETHICS MANUAL, *supra* note 118; *see* SENATE ETHICS MANUAL, *supra* note 118.

131. U.S. CONST. art. I, § 5, cl. 2 (providing that "Each House may determine the Rules of its Proceedings, punish its Members for disorderly Behavior, and with the Concurrence of two-thirds, expel a Member.").

132. 166 U.S. 661 (1897).

133. *Id.* at 669–70; *see* Nagy, *supra* note 128, at 1143 (observing that while Congress is often criticized for its reluctance to self-discipline its members—with the reluctance extending to even relatively mild sanctions involving denouncement or reprimand—there is no doubt that each chamber "has the authority to proscribe and sanction betrayals of the public trust"); *see also* Theresa A. Gabaldon, *The Self-Regulation of Congressional Ethics: Substance and Structure*, 48 ADMIN. L. REV. 39, 46 (1996) (observing that at least one senator has been censured for actions "derogat[ing] from the public trust expected of a senator" even though the conduct at issue had not violated "any specific law or rule in force at the time").

134. 130 S. Ct. 2896 (2010).

135. *Id.* at 2929–30 (citing United States v. Diggs, 613 F.2d 988, 998 (D.C. Cir. 1979)).

136. 613 F.2d 988 (D.C. Cir. 1979).

137. *Id.* at 998.

138. 572 F.2d 31 (2d Cir. 1978).

States Congressman."[139] Relying on equitable principles rather than on an express statutory remedy for his violation of a conflict-of-interest statute, the court regarded the congressman's receipt of compensation and campaign contributions—for his appearances before several federal agencies on behalf of an airline—as ill-gotten gains that he held "in constructive trust for the government."[140]

Yet when we turn to the federal statutes and ethics rules that govern members and employees of Congress and we shift our focus specifically to financial conflicts of interest arising from personal investments, the fiduciary dictates that we would expect to see are nowhere to be found. Instead, except in the limited circumstances of earmarks,[141] we mainly find commentary in ethics manuals setting forth rationalizations for the absence of such dictates.[142] The dearth of ethics rules regulating personal investments (not to mention the total absence of a judicially enforceable statute) is particularly striking when compared to the strict financial conflict-of-interest restraints that Congress has placed on executive and judicial branch officials and the heightened scrutiny that state corporate law accords to interested-director transactions. Although limitations on the type of securities that lawmakers can own may discourage some persons from pursuing or continuing with congressional service, others may be even more drawn to serve in an institution that commits itself to higher standards of ethics and fiduciary principles.

B. Congressional Rules and Rationales Relating to Financial Conflicts

1. The Senate

Rule 37, paragraph 4 of the Senate Code of Official Conduct is the ethical provision that is said to prohibit senators from using their legislative power to advance their own personal financial interests. It states that

> [n]o Member, officer, or employee shall knowingly use his official position to introduce or aid the progress or passage of legislation, a principal purpose of which is to further only his pecuniary interest, only the pecuniary interest of his

139. *Id.* at 32.

140. *Id.* at 34–35. The court observed that the congressman previously had pleaded guilty to charges involving conspiracy to violate 18 U.S.C. § 203 as well as a substantive violation of that conflict-of-interest statute and had been sentenced to two years in prison, eighteen months of which had been suspended, for the conspiracy count and fined $5,000 on the conflict-of-interest count. *Id.* at 34. For additional analysis of the *Podell* decision, see *House STOCK Act Hearing*, *supra* note 119, at 57 (testimony by Jack Maskell).

141. *See infra* Subpart III.B.3.

142. SENATE ETHICS MANUAL, *supra* note 118, at 69.

> immediate family, or only the pecuniary interest of a limited class of persons or enterprises, when he, or his immediate family, or enterprises controlled by them, are members of the affected class.[143]

The Senate Ethics Manual, which is published by the Senate Select Committee on Ethics (the "Ethics Committee"), expressly describes Rule 37(4)'s scope as "narrow."[144] It also candidly acknowledges that "[l]egislation may have a significant financial effect on a senator because his holdings are involved."[145] But as long as that legislation "has a broad, general impact on his state or the nation," Rule 37(4) would not prevent a senator from voting on the legislation or from playing an active role in advancing or blocking its passage.[146]

The plain language of Rule 37(4)'s prohibition, which turns in large part on the lawmaker's motive, reveals why the rule is actually more akin to an anticorruption rule than an anticonflicts rule. To violate Rule 37(4), a senator would not only have to "know" that the legislation in question would advance his (or an immediate family member's) "pecuniary interest," but his action to "introduce or aid the process or passage" of that legislation also must have had as its "principal purpose" the furthering of "only" his or his family's pecuniary interest or "only" the pecuniary interests of a "limited class" in which he is a member. If his actions were intended to further several interests of equivalent importance, only one of which was self-serving, then the rule's "principal purpose" prong would not be met.

Rule 37(4) dates back to 1977, a few years after Watergate, when the Senate amended its Standing Rules to include a Code of Official Conduct. Senator Gaylord Nelson (D-Wis.) chaired the special committee (now referred to as the "Nelson Committee") that proposed the code. To illustrate the restrictive scope of this new prohibition, the Nelson Committee included in its report an example involving a dairy farmer from a state with dairy as a leading industry.[147] In the Nelson Committee's view, this senator could

---

143. SELECT COMM. ON ETHICS, 110TH CONG., SENATE CODE OF OFFICIAL CONDUCT 16 (Comm. Print 2008). Senate Rule 37(1) provides more generally that "[a] Member, officer, or employee of the Senate shall not receive any compensation, nor shall he permit any compensation to accrue to his beneficial interest from any source, the receipt or accrual of which would occur by virtue of influence improperly exerted from his position as a Member, Officer, or employee." *Id.*

144. SENATE ETHICS MANUAL, *supra* note 118, at 69.

145. *Id.*

146. *Id.*

147. S. SPECIAL COMM. ON OFFICIAL CONDUCT, SENATE CODE OF OFFICIAL CONDUCT, S. REP. NO. 95-49, at 42 (1977) [hereinafter NELSON COMMITTEE REPORT]. The Report identified a substantially similar version of what is now Rule 37(4) as then Rule 45(4). *See id.* at 41.

introduce, work for, and vote for the passage of a bill that would boost or maintain price supports for milk products, while "not fall[ing] under the strictures of this Rule."[148] As the Nelson Committee explained:

> The strong presumption would be that the Member was working for legislation because of the public interest and the needs of his constituents and that his own financial interest was only incidentally related. In the terminology of [Rule 37(4)], the dairy farmer would be part of a class affected by the legislation, but not a member of a "limited class." . . . [A] class of people or enterprises sharing a particular economic interest (i.e. dairy farmers; shoemakers; disabled veterans) would not be a "limited class."[149]

The Nelson Committee went on to emphasize that Rule 37(4)'s reference to "limited class" was intended to mean "the class of people affected by a *private* bill."[150] Thus, while the dairy farm senator could push for the passage of price supports that benefit himself and his constituents, he could not introduce or work for the passage of legislation "to purchase a piece of land made up in part of a piece of his property and in part of pieces of his neighbors' property, in order to build a federal project there."[151] Thus, as the Nelson Committee envisioned, the prohibition in Rule 37(4) "addresses itself to the *rare* case when the relationship between the legislator's private interest and the public interest is dramatically different from the ordinary situation."[152]

Legislation that affects publicly traded companies, and thereby the value of a company's stock, is anything but a rare instance. Thus, the same analysis that applied to the dairy farmer would apply, for example, to a senator who owns a sizable amount of stock in AT&T. (In 2011, fifty-two members of Congress reported holdings in AT&T stock, at least six with holdings exceeding $100,000.)[153] Despite stock investments that might create a conflict of interest, that senator could push for wireless network legislation strongly favoring large telecommunication providers because such companies

---

148. *Id.* at 42.
149. *Id.*
150. *Id.* (emphasis added).
151. *Id.*; *see infra* text accompanying notes 221–23 (comparing Senate Rule 37(4) with Standing Rule 44(6), which governs financial interests in the context of earmarks and limited tax benefits).
152. NELSON COMMITTEE REPORT, *supra* note 147 (emphasis added).
153. Ctr. for Responsive Politics, *Most Popular Congressional Investments, 2011*, OPENSECRETS.ORG, http://www.opensecrets.org/pfds/overview.php?type=P&year=2011 (last visited June 26, 2013).

and their shareholders hardly constitute a "limited class."[154] Even if that senator were acting for the "principal purpose" of increasing profits for AT&T (a motivation that would be next to impossible to show), the millions of shareholders in AT&T likely would not qualify as a "limited class."[155] And the Senate Manual leaves no doubt that "[b]oth the 'principal purpose' and the 'limited class' test must be met before [Rule 37(4)] precludes a Senator's involvement in a legislative proposal."[156] As such, Rule 37(4) plainly fails to capture many of the securities investments that could possibly tempt a senator toward self-interested decision making and away from his fiduciary obligations.

Indeed, if this senator's actions were held to fiduciary standards, the public would be freed from speculating about whether his personal stock holdings in AT&T had influenced his wireless network advocacy entirely, or substantially, or somewhat, or not at all. The conflict component of a fiduciary obligation would prohibit the senator from placing himself in a position in which he might be tempted to place his own pecuniary interests ahead of the public. Thus, in view of his sizeable stock holdings in AT&T, the senator would have no choice but to refrain from working on the wireless network legislation (and arguably from voting on it as well). Beyond that, the avoidance component would constrain the senator's ability to hold stocks that risked impairing his legislative responsibilities. Thus, a substantial investment in AT&T would be verboten if he were a member of the Senate Committee on Commerce, Science, & Transportation ("CS&T"), and particularly so if he served on the Communications, Technology, and the Internet Subcommittee. Arguably, any investment in the stock of AT&T would be impermissible under fiduciary principles given the size of that multinational corporation and the frequency with which it has interests before Congress.

Yet, the Senate's view that such fiduciary rules are unwarranted for lawmakers has not stopped it from imposing those

154. *Cf.* SENATE ETHICS MANUAL, *supra* note 118, at 70 (observing that the Senate Ethics Committee had ruled in 1990 that "a Senator who owned shares in a company that owed cable stations could participate in legislation directly affecting cable companies"). The senator could also support legislation awarding a government contract to AT&T. Although 18 U.S.C. § 431 prohibits members of Congress from entering into or benefitting from contracts with the federal government, government contracts with "any incorporated company for the general benefit of such corporation" are exempt from this provision. 18 U.S.C. § 433 (2006).

155. *See infra* text accompanying note 179 (discussing precedent in House Ethics Manual involving appropriations for a project undertaken by a single defense contractor in which a member owned a small fraction of widely traded shares).

156. SENATE ETHICS MANUAL, *supra* note 118, at 69.

rules on government officials in the executive and judicial branches. An attorney at the FCC could not work on a new regulation for wireless networks if she were to own a substantial amount of stock in AT&T (in fact, federal law would bar her from investing in any telecommunications firm),[157] and a federal judge who owned stock in AT&T could not oversee a proceeding challenging an FCC broadband regulation. In the absence of their respective recusal, the FCC official could face criminal charges and the federal judge could be disciplined, even if their financial interests were exceedingly unlikely to influence their decision making and even if the officials sincerely believed that their actions could be completely fair and impartial.[158]

Nor is the Senate's own presumption of virtuous decision making carried forward to its legislative staffers, at least with respect to staffers employed by Senate committees. In 1977, the Nelson Committee recommended and the Senate adopted Rule 37(7), which provides that

> [a]n employee on the staff of a committee. . . shall divest himself of any substantial holdings which may be directly affected by the actions of the committee for which he works, unless the Select Committee, after consultation with the employee's supervisor, grants permission in writing to retain such holdings or the employee makes other arrangements acceptable to the Select Committee and the employee's supervisor to avoid participation in committee actions where there is a conflict of interest, or the appearance thereof.[159]

In the view of the Nelson Committee, such disparate treatment was justified because

> unlike Senators, committee staff are not publicly accountable, and despite public financial disclosure, their affairs are unlikely to get the same kind of scrutiny from the public and the press as Senators. At the same time, committee staff members hold responsible positions. For these reasons, the Committee believes that staff holdings should be treated with particular care.[160]

---

157. 47 U.S.C. § 154(b)(2)(A)(ii) (2006) (prohibiting FCC officials from holding investments in telecommunications companies).

158. *See id.*

159. Senate Rule 37, § 7, *reprinted in* SENATE ETHICS MANUAL, *supra* note 118, at 322. By its terms, the rule applies only to committee staff earning more than "$25,000 per annum and employed for more than ninety days in a calendar year." *Id.*

160. NELSON COMMITTEE REPORT, *supra* note 147, at 44.

Thus, absent special permission, a staffer employed by the CS&T Committee could not hold a sizeable amount of stock in AT&T, even if that staff member focused his own work entirely on oceans and fisheries and lacked any discretion over decisions concerning telecommunications. As such, Senate Rule 37(7) goes beyond what fiduciary analysis would require.

Recall the Supreme Court's observation of the "evil" to which statutory restraints on financial interests is directed.[161] A legislative effort that increases a lawmaker's wealth by substantially affecting the value of a publicly traded company's stock would certainly seem to constitute an activity "which arouse[s] suspicions of malfeasance and corruption."[162] Such an action thus "endangers the very fabric of a democratic society" by shattering the people's "faith in those who govern."[163]

The Nelson Committee, however, was confident that the twin mechanisms of financial disclosure and electoral accountability were adequate safeguards against self-interested decision making by lawmakers. For that reason, then, the Committee

> resisted suggestions for elaborate schemes which would have required that Senators not serve on certain committees, or disqualify themselves from voting in every case when their holdings or investments could pose a conflict of interest. No Rule suggested to the Committee avoided conflicts without totally undermining the Senator's ability to represent the interests of his constituents. Consequently, the Committee concluded that financial disclosure of all holdings and possible conflicts was a preferable approach.[164]

As we will see, among the Committee's "resisted suggestions" was one by the NYCBA for a congressional rule requiring lawmakers to "avoid all economic interests which may be specifically affected by legislation within the jurisdiction of [their] committee[s]."[165]

The Senate Manual leaves no doubt that the Nelson Committee's expressed faith in financial disclosure and the electoral process continues right up to the present. A rule requiring recusal, as the Manual explains, would compromise the interests of the lawmaker's constituents because

> [t]hose who elect Senators and Congressmen are entitled to have their elected representatives represent them by voting and fully participating in all aspects of the legislative process.

---

161. United States v. Miss. Valley Generating Co., 364 U.S. 520, 562 (1961).
162. *Id.*
163. *Id.*
164. NELSON COMMITTEE REPORT, *supra* note 147, at 4; *accord id.* at 10.
165. NYCBA 1970 REPORT, *supra* note 16, at 68.

> This representation is carried out with the understanding that the votes cast by the Senators and Congressmen are predicated on their perceptions of the public interest and the public good, not on personal pecuniary interest.[166]

The Manual also emphasizes that "even a selective divestiture of potentially conflicting assets is not required," in large part because public disclosure "provide[s] the information necessary to allow Members' constituencies to judge official conduct in light of possible financial conflicts with private holdings."[167] These rationales for the differences across the three branches will be fully explored in the Subpart that follows.

Before turning to that analysis, a final observation can be made here. Senate Rule 37(4) and the ethical norms that stem from it reveal a striking contrast between the loyalty obligation that Congress envisions for itself and the duty of loyalty that operates in corporations. When personal financial interests are involved, political judgments by congressional officials are substantially more insulated from scrutiny than business judgments by corporate officials. Directors who stand to gain personally from a corporate transaction are denied any type of presumption, strong or otherwise, that their votes are, in the words of the Nelson Committee, "predicated on their perceptions . . . of the [corporation's] good, not on personal pecuniary interest."[168] Thus, in this regard at least, corporate law takes fiduciary principles much more seriously.

2. *The House of Representatives*

Like the Senate, the ethics rules in the House are not tailored toward avoiding (let alone eliminating) financial interests that could possibly tempt lawmakers to favor their own pecuniary interests ahead of the public they serve. The principal guard against self-interested conduct by members of the House is Rule 23, paragraph 3 of the House Code of Official Conduct, which specifies that

> [a] Member, Delegate, Resident Commissioner, officer, or employee of the House may not receive compensation and may not permit compensation to accrue to the beneficial interest of such individual from any source, the receipt of which would occur by virtue of influence improperly exerted from the position of such individual in Congress.[169]

---

166. SENATE ETHICS MANUAL, *supra* note 118, at 69.
167. *Id.* at 124–25.
168. *See supra* note 147.
169. CONSTITUTION, JEFFERSON'S MANUAL, AND RULES OF THE HOUSE OF REPRESENTATIVES, H.R. Doc. No. 112-161, at 934–35, para. 3 (2013) [hereinafter HOUSE RULES] (Rule 23).

The commentary in the House Ethics Manual, which is compiled by the House Committee on Standards of Official Conduct (the "Standards Committee"), clarifies that this provision governs aspects of the "investments of House Members and employees."[170] And the manual expressly states that "all Members, officers, and employees are prohibited from improperly using their official positions for personal gain."[171] But after quoting the NYCBA's astute observation that "[m]uch distrust of government flows from ambiguous circumstances where there is ground for suspicion that officials are promoting their own welfare rather than the public's,"[172] the Manual observes that

> [a]s a general matter . . . Members and employees need not divest themselves of assets upon assuming their positions, nor must Members disqualify themselves from voting on issues that generally affect their personal financial interests. Instead, public financial disclosure provides a means of monitoring and deterring conflicts.[173]

That rather unambiguous message is followed by this statement: "[n]o federal statute, regulation, or rule of the House absolutely prohibits a member or House employee from holding assets that might conflict with or influence the performance of official duties."[174]

In addition to House Rule 23(3), a representative's financial conflicts must be evaluated under House Rule 3, which provides that "[e]very Member . . . shall vote on each question put, unless he has a direct personal or pecuniary interest in the event of such question."[175] Longstanding House precedents, however, emphasize that financial interests are disqualifying only when a member's vote affects him or her directly as an individual and not merely as one of a class.[176] The Manual provides the following examples:

> Members holding stock in national banks have voted on legislation "providing a national currency and to establish free banking" since Members "do not have that interest separate

170. HOUSE ETHICS MANUAL, *supra* note 118, at 248.
171. *Id.* at 247.
172. *Id.* (quoting NYCBA 1970 REPORT, *supra* note 16, at 34).
173. *Id.* at 247.
174. *Id.* at 248.
175. HOUSE RULES, *supra* note 169, at 377 (Rule 3). The closest Senate analogue to House Rule 3 is Senate Rule 12(3), which provides that a senator "may decline to vote in committee or on the floor, on any matter when he believes that this voting on such a matter would be a conflict of interest." *See* SENATE MANUAL CONTAINING THE STANDING RULES, ORDERS, LAWS, AND RESOLUTIONS AFFECTING THE BUSINESS OF THE UNITED STATES SENATE, S. Doc. 112-1, at 12, para. 3 (2011) [hereinafter SENATE RULES] (Rule 12).
176. HOUSE ETHICS MANUAL, *supra* note 118, at 235.

> and distinct from a class, and, within the meaning of the rule, distinct from the public interest." . . . The Speaker would not rule that a Member owning stocks in breweries or distilleries should be disqualified in voting on the proposed amendment to the Constitution concerning prohibition of the manufacture and sale of liquor. Members who were stockholders in or had interests in import businesses voted on a tariff bill affecting the import business since "the bill before us affects a very large class. . . . The Chair would be surprised if there were not hundreds of thousands of American citizens who were stockholders in these companies . . . ."[177]

Although both the House and the Senate construe their respective rules to foreclose certain legislative activities that produce pecuniary benefits for a "limited class" in which a lawmaker is a member, House Rule 3 does not explicitly impose the same "principal purpose" qualifier that appears in Senate Rule 37(4). But it is possible that a qualifier grounded in a lawmaker's motivation applies to House Rule 3 implicitly. For example, with no reference at all to the lawmaker's reason(s) for supporting a bill, the Manual suggests that Rule 3's voting disqualification for a pecuniary interest "*might* apply if legislation affects only one specific business or property, rather than a class or group of businesses or properties."[178] But in contravention, the Manual points to a more recent precedent where the Standards Committee found that a congressman's ownership of common stock in a defense contractor corporation (1,000 shares out of more than 4.5 million outstanding) was insufficient "'to disqualify him from voting on' an appropriations bill authorizing funds for a project for which the corporation was under contract with the government to perform."[179] The different conclusions contemplated by the Manual could perhaps have turned on the lawmaker's "principal purpose." An insubstantial number of shares in a widely traded corporation could negate an inference that

177. *Id.* (second alteration in original) (quoting House precedents).

178. *Id.* (emphasis added) (citing, among other instances, a 1907 precedent suggesting that if a member's vote were to be challenged, the chair should hold that he lacked the right to vote on a bill specifically related to Central Pacific Railroad, in view of his ownership of stock in that railroad).

179. *Id.* at 237 (quoting IN THE MATTER OF A COMPLAINT AGAINST REP. ROBERT L.F. SIKES, H.R. REP. NO. 94-1364, at 15 (1976)). The Standards Committee found, however, that the congressman had wrongly used his official position for personal benefit on two other occasions: when he "persuaded the organizers of a privately held bank to sell him stock while he was using his congressional position to promote authorization for the establishment of the bank" and when he "sponsored legislation to remove restrictions on the development of property in which he had a personal financial interest." HOUSE ETHICS MANUAL, *supra* note 118, at 186. The congressman was ultimately reprimanded by the House. *See id.* at 249.

pecuniary gain was a principal purpose behind a decision to support (or disfavor) a bill.

The House Manual acknowledges that sponsoring legislation, committee participation, and contacting officials at executive agencies entail "a degree of advocacy above and beyond that in voting" and it observes that such activities require "added circumspection" on the part of members as to whether they may take such actions in view of their financial interests.[180] The Standards Committee advises members to consult with it for guidance whenever they are "considering taking such action on a matter that may affect [their] personal financial interests," and it references in particular the rules and standards that "prohibit the use of one's position for personal gain."[181] But ethics experts and government watchdog groups have been critical of the House Standards Committee (and the Senate Ethics Committee as well) for providing advisory opinions that typically "give support and justification to lawmakers who take actions that intersect with their personal financial holdings."[182] Ethics experts are also quick to point out the rarity of congressional self-discipline for legislative actions relating to personal financial interests.[183]

As in the Senate, the House's current rules and norms pertaining to financial investments are rooted in decisions that were made in 1977. In the House, the analogue to the Nelson Report was a report based on the recommendations of the House Commission on Administrative Review's Task Force on Financial Ethics, which was chaired by then-Congressman Lee Hamilton (D-Ind).[184] And like the Nelson Committee in the Senate, this House Commission considered various approaches to conflicts that would have required lawmakers "either to divest themselves of holdings which might cause potential conflicts of interest or be disqualified from voting on issues which affect their investments."[185] Finding "serious drawbacks" with such approaches, the Commission concluded that

> [i]n the case of investment income, then, the Commission's belief is that potential conflicts of interest are best deterred through disclosure and the discipline of the electoral process. Other approaches are flawed both in terms of their

180. *Id.* at 237.

181. *Id.*

182. *See* Kindy, et al., *supra* note 5.

183. *See Insider Trading and Congressional Accountability: Hearing Before the S. Comm. on Homeland Sec. & Gov't Affairs*, 112th Cong. 9–10 (2011) [hereinafter *Senate STOCK Act Hearing*] (testimony of Melanie Sloan, Executive Director, Center for Responsible Ethics in Washington ("CREW")).

184. *See* HOUSE COMM'N ON ADMIN. REVIEW, FINANCIAL ETHICS, H. DOC. 95-73, at 9–10 (1977).

185. *Id.* at 9.

> reasonableness and practicality and threaten to impair rather than to protect the relationship between the representative and the represented.[186]

The House Commission's strong preference for enhanced financial disclosure in lieu of anticonflict restraints (which was echoed by the Senate's Nelson Committee) materialized the following year in the Ethics in Government Act of 1978. The EIGA converted existing congressional rules on financial disclosure into stricter and more encompassing statutory requirements.[187] A decade later, a House Bipartisan Task Force on Ethics concluded that the EIGA was achieving its anticonflicts objective:

> The task force believes, in light of the ten year history of the disclosure law under the Ethics in Government Act, that public financial disclosure, coupled with the discipline of the electoral process, remains the best safeguard and the most appropriate method to deter and monitor potential conflicts of interest in the legislative branch.[188]

Whether public disclosure and electoral discipline are adequate safeguards against self-interested legislative activity (let alone "the best") is a question that has received surprisingly little scrutiny from legal scholars. One important exception is Professor Richard Painter, who recognizes that congressional concerns about the effect of recusal on the process of democratic representation are legitimate. But he emphasizes the other important democratic values that are at stake as well. He therefore advocates a balancing test, of sorts:

> Preserving a member's power to sponsor and vote on legislation is important, but public confidence in the integrity of government is also important. The effect on legislative process from a handful of members in the House or Senate recusing on a bill would in most cases be less harmful than a public perception that members are participating in matters in which they have significant financial interests. Congress should be willing to abide by, at least in its own rules if not a criminal statute, a standard that is more similar to that which it imposes on the executive branch.[189]

Disqualification, moreover, is hardly the only way fiduciaries can fulfill their duty of loyalty to their entrustors. Indeed, if ethics

---

186. *Id.* at 9–10. The House Manual quotes the Commission's conclusion verbatim. HOUSE ETHICS MANUAL, *supra* note 118, at 251.

187. *See supra* notes 59–64 and accompanying text.

188. BIPARTISAN TASK FORCE ON ETHICS, 101ST CONG., REP. ON H.R. 3660, 22 (Comm. Print 1989).

189. PAINTER, *supra* note 3, at 148.

rules and norms in Congress were to reflect the avoidance component of a fiduciary obligation, concerns about diminution of citizen voice and power would not even be implicated.

The House Manual, however, continues to depict the divestiture alternative to recusal as both "impractical" and "unreasonable."[190] It elaborates:

> Members of Congress enter public service owning assets and having private investment interests like other citizens. Members should not "be expected to fully strip themselves of worldly goods." Even a selective divestiture of potentially conflicting assets could raise problems for a legislator. Unlike many officials in the executive branch, who are concerned with administration and regulation in a narrow area, a Member of Congress must exercise judgment concerning legislation across the entire spectrum of business and economic endeavors. Requiring divestiture may also insulate legislators from the personal and economic interests held by their constituencies, or society in general, in governmental decisions and policy.[191]

The "worldly goods" quote was drawn from the NYCBA's 1970 Report on congressional ethics, which included an unequivocal recommendation for a divestiture rule, akin to the rule now governing Senate Committee staffers.[192]

Particularly in the context of today's lawmakers and their current financial investments, each of the concerns set out in the House Manual regarding conflict avoidance through divestiture rings hollow. Even a complete prohibition against holding stocks or bonds in individual companies would allow lawmakers to retain most other types of "worldly goods," including shares in diversified mutual funds. Moreover, while lawmakers necessarily function as generalists when casting floor votes on a bill, much discretionary decision making occurs at the committee level, where lawmakers function much more as specialists charged with overseeing particular industries.

Concerns about "insulating" members from constituent interests can be easily dismissed as well. A legislator from Wisconsin should be able to zealously represent the interests of dairy farmers without having his own personal wealth invested in livestock and farm equipment. But even if an argument based on the value of "merged" interests is valid in the context of some financial investments (the citizens of Texas may wish—and may well be entitled—to send oilmen to Washington), that argument loses traction with respect to a lawmaker's passive investments in securities issued by publicly

190. HOUSE ETHICS MANUAL, *supra* note 118, at 249–50.
191. *Id.* at 250 (quoting NYCBA 1970 REPORT, *supra* note 16, at 40).
192. *See infra* Subpart IV.B.1.

traded corporations. Owning portfolios with hundreds of thousands of dollars invested in the stock of General Electric, J.P. Morgan, and other multinational companies brings the typical lawmaker no closer to the interests of his constituents than a portfolio with shares in mutual funds that invest in those very same companies.

The remaining argument set out in the House Manual against a divestment rule relates to the "discipline" that is said to be imposed by the electoral process. To be sure, the EIGA's statutory scheme for financial disclosure serves to inform the public about possibly conflicting interests. And stories in the media help voters understand and appreciate the possible connections between a particular lawmaker's investment holdings and his or her legislative activity.[193] Yet, despite such transparency, the electoral process has not proven to be a particularly effective vehicle for controlling possibly self-serving legislative conduct, at least conduct which falls short of serious corruption (leaving aside the numerous lawmakers who have been reelected despite charges involving serious corruption).[194] Officeholders in Congress clearly "have an advantage over anyone who challenges their authority."[195]

Not only is reliance on the electoral process to reduce conflicts an ineffective approach in practice, but it is also "deficient in principle."[196] The beneficiaries of an individual lawmaker's duty of loyalty include not only those who voted for her but also the general public. A lawmaker's actions on a congressional committee and any leadership role she fulfills in the House or Senate impact the entire nation. As Professor Dennis Thompson, a leading political science scholar, points out:

> Because legislative ethics provides . . . the preconditions for all legislative action, citizens rightly take an interest in the ethical conduct of all members, not only that of their own representatives. In this respect their concern about ethical conduct differs from their interest in any particular piece of legislation. Even on delegate conceptions of democratic representation, constituents in *any* state or district may quite properly instruct their representative to seek, through procedures of the representative assembly, standards to govern the ethical conduct of *all* representatives. That is part of the rationale for the disciplinary authority of the ethics

---

193. *See generally supra* note 5 (citing front-page news articles); *see also infra* text accompanying notes 232–42.

194. PAINTER, *supra* note 3, at 8–10.

195. *Id.* at 5.

196. DENNIS F. THOMPSON, ETHICS IN CONGRESS: FROM INDIVIDUAL TO INSTITUTIONAL CORRUPTION 137 (1995).

> committees and ultimately for Congress's constitutional power of expulsion.[197]

Thus, "letting members disclose and voters decide" is a defense of the status quo that is grounded in a "mistaken view of democratic representation."[198]

Once again, an analogy to the corporate world is instructive. Under the corporate law of every state, directors are chosen by a vote of the corporation's shareholders. But corporate law does not look solely to elections to guard against agency problems such as conflicted decision making on the part of directors.[199] Instead, the fiduciary duty of loyalty performs much of that work. As the Delaware Supreme Court emphasized in *Guth v. Loft*,[200] "[t]he rule that requires an undivided and unselfish loyalty to the corporation demands that there shall be no conflict between duty and self-interest."[201] Section 144(a)(2) does provide a mechanism by which shareholders in Delaware may effectively waive the protections of the fiduciary obligation that is owed to the corporation.[202] But section 144(a)(2) is a transaction-specific provision that requires a majority of disinterested shareholders to vote in good faith, after full disclosure of the interested director's conflict, in favor of the transaction. Even if all potential conflicts had been fully disclosed to shareholders in a proxy statement, a director's election (even by the vote of a majority of disinterested shareholders) would not serve to sanitize all interested-director transactions proposed in the future. Shareholder votes on each separate interested-director transaction would be necessary. And, in the absence of such a vote by shareholders, the fiduciary rule that requires undivided and unselfish loyalty to the corporation would not be deemed to have been waived.

3. *The Special Case of Earmarks*

Interestingly, in both the House and the Senate, financial conflicts of interest are subject to a special rule when the legislative activity at issue involves a congressional earmark, a limited tax benefit, or a limited tariff benefit (often referred to collectively as "earmarks").[203] Made (in)famous by frequent references in the media to a $223 million "Bridge to Nowhere," earmarks are typically

---

197. *Id.* at 138.
198. *Id.* at 137.
199. Rave, *supra* note 3, at 676–77.
200. 5 A.2d 503 (Del. 1939).
201. *Id.* at 510.
202. *See supra* text accompanying note 34; *see also* DEL. CODE ANN. tit. 8, § 144(a)(2) (2011).
203. *See* Rebecca M. Kysar, *Listening to Congress: Earmark Rules and Statutory Interpretation*, 94 CORNELL L. REV. 519, 521 & n.6 (2009).

defined as a targeted spending request by one, and sometimes two or more, members of Congress for a particular project or beneficiary.[204] The earmark "is often inserted in the latter stages of a bill's journey through Congress, generally in the accompanying committee report."[205]

Agency problems redound in the legislative process that results in earmarks. Even though taxpayers generally understand that the sum total of funds expended on targeted projects can usually be spent more efficiently in a manner that aligns more closely with national priorities, anticipated campaign contributions from lobbyists and the immediate beneficiaries of earmarks often sway lawmakers to sponsor them—even for projects located outside of their own state or district.[206] While Congress is unlikely to enact a permanent ban on legislative earmarks, both chambers in recent years have instituted temporary moratoriums as part of a series of measures to control deficit spending.[207]

The firestorm against earmarks began to ignite in the mid-2000s after investigatory reports in the media spotlighted wasteful spending in general and earmark abuses in particular.[208] The public backlash, fueled with activism by CREW and other government watchdog groups, prompted Congress in 2007 to reform the earmark process by increasing transparency and accountability.[209] Pursuant to these reforms, lawmakers who request earmarks are required to file written statements (easily accessible to the public) that disclose: the lawmaker's name; the name and address of the intended recipient of an earmark (or the location of the intended activity if there is no intended recipient); the name of the beneficiary in the case of a limited tax or tariff benefit; the purpose of the earmark or limited tax or tariff benefit; and a certification that neither the

---

204. PAINTER, *supra* note 3, at 153 (observing that the proposed Gravina Island Bridge in Alaska was an earmark sponsored by Senator Ted Steven (R-AK)).

205. *Id.*

206. *Id.* at 155 (discussing press reports about a $10 million highway interchange project in Florida promoted by a congressman in Alaska).

207. *See* Fawn Johnson, *Does the Earmark Moratorium Hurt Congress?*, NATIONALJOURNAL (Aug. 26, 2013, 8:30 AM), http://www.nationaljournal.com/insiders/transportation/does-the-earmark-moratorium-hurt-congress-20130826; Manu Raju, *Earmarks Aren't Gone for Good*, POLITICO (Jan. 5, 2011 4:40 AM), http://www.politico.com/news/stories/0111/47063.html.

208. *See* Melanie Sloan, *Earmark Reform: Building a Bridge to Somewhere, The Blog*, HUFFINGTON POST (Oct. 7, 2010, 9:45 AM), http://www.huffingtonpost.com/melanie-sloan/earmark-reform-building-a_b_753962.html (discussing five-point plan "to clean up the congressional earmarking process").

209. *See* Kysar, *supra* note 203, at 534–35 (discussing the political factors that precipitated the adoption of earmark rules).

member nor certain related persons has a pecuniary interest in the earmark or limited tax or tariff benefit.[210]

The certifications required under the earmark rules in both chambers appear similar at first blush, but there are differences that may be significant. House Rule 23, paragraph 17 of the House Code of Official Conduct requires

> [a] Member . . . who requests a congressional earmark, a limited tax benefit, or a limited tariff benefit in any bill or joint resolution (or an accompanying report) or in any conference report on a bill or joint resolution (or an accompanying joint statement of managers) . . . [to] provide a written statement to the chair and ranking minority member of the committee of jurisdiction, . . . that . . . [certifies] that the Member . . . or spouse has no financial interest in such congressional earmark or limited tax or tariff benefit.[211]

Committees with jurisdiction over a particular earmark or tax benefit request are responsible for determining whether Rule 23(17)'s heightened disclosure requirements (including the "no financial interest" certification) are triggered.[212]

Whether a member of the House (and/or a spouse) has a "financial interest" in an earmark depends on his or her particular financial circumstances and the specific facts surrounding the request.[213] But the House Manual observes that

> [a]s a general matter, a financial interest would exist in an earmark when it would be reasonable to conclude that the provision would have a direct and foreseeable effect on the pecuniary interests of the Member or the Member's spouse. *Such interests may be related to financial assets, liabilities, or other interests of the Member and spouse, such as investments in stocks, bonds, mutual funds, or real estate.*[214]

An "effect is foreseeable if it is anticipated or predictable."[215] The House Manual also quotes (presumably by analogy) the OGE regulation that defines the term "predictable" for purposes of the federal statute that criminalizes conflicts of interest for the executive branch.[216] Direct and foreseeable effects on a House

---

210. *See* HOUSE RULES, *supra* note 169 at 942–43, para. 17 (Rule 23); SENATE RULES, *supra* note 92 at 175, para. 6 (Rule 44).

211. *Id.*

212. HOUSE ETHICS MANUAL, *supra* note 118, at 238.

213. *Id.*

214. *Id.* at 239 (emphasis added).

215. *Id.* at 239 n.108

216. *Id.* at 239 (quoting 5 C.F.R. § 2640.103(a)(3)(ii) (2012)). Section 2640.103(a)(3)(ii) "defin[es] the term 'predictable' as 'real, as opposed to a speculative possibility that the matter will affect the financial interest.'" *Id.*

member's (or spouse's) pecuniary interests are contrasted explicitly with financial interests that are "remote, inconsequential, or speculative."[217] Two differing situations are depicted:

> For example, if a Member proposed an earmark or tax or tariff benefit assisting a certain company, the Member generally would not be considered to have a financial interest in the provision by owning shares in a diversified mutual fund, employee benefit plan (*e.g.*, the Thrift Savings Plan or similar state benefit plan), or pension plan that, in turn, holds stock in the company. *However, a Member's direct ownership of stock, even a small number of shares in a widely held company, likely would constitute a financial interest under Rule 23.*[218]

The 2007 earmark reform in the House therefore appears to have altered the conventional financial conflict-of-interest analysis, at least to a certain extent. Consider, for example, a lawmaker who owns $50,000 of stock in Dynamic Defense Corp. ("DD Corp.") and is contemplating an earmark request directed at DD Corp. for several million dollars in funding to assist its development of a new type of body armor for the military. Before the reforms took effect, little would have prevented the lawmaker from requesting such an earmark, even if he had owned thousands of dollars in DD Corp. stock. Indeed, it is not at all clear that the request would have violated the House rule that proscribes personal gain from legislative activity,[219] and even if the request were in fact improper, there is little chance that the lawmaker's conflict would have even been detected, let alone become the fodder for a congressional disciplinary proceeding. Now, however, with House Rule 23(17)'s certification requirement in place, that lawmaker would be unable to file a truthful statement that he had "no financial interest in such congressional earmark." Thus, Rule 23(17) would foreclose his earmark request (or require divestment) and, at least in this instance, eliminate the financial conflict of interest.

In the Senate, however, one can reasonably question whether the "special" financial conflict-of-interest rule that applies to earmarks alters the conventional analysis, even to a limited degree. The Senate adopted its version of an earmark certification rule as part of the Honest Leadership and Open Government Act of 2007.[220] The Act added a new Rule 44, paragraph 6, to the Standing Rules of the Senate, which provides:

217. *Id.*

218. *Id.* (emphasis added).

219. *See supra* text accompanying note 169 (quoting House Rule 23(3)).

220. Honest Leadership and Open Government Act of 2007, Pub. L. No. 100-81, § 521, 121 Stat. 735, 760–64.

> A Senator who requests a congressionally directed spending item, a limited tax benefit, or a limited tariff benefit in any bill or joint resolution (or an accompanying report) or in any conference report on a bill or joint resolution (or an accompanying joint statement of managers) shall provide a written statement to the chairman and ranking minority member of the committee of jurisdiction, . . .[that certifies] that neither the Senator nor the Senator's immediate family has a pecuniary interest in the item, ***consistent with requirements of paragraph 9***.[221]

In the absence of the italicized language, Senate Rule 44(6) would closely resemble the "no financial interest" certification requirement in the House, except that it more broadly encompasses a lawmaker's immediate family members (a term which includes children and parents as well as a spouse). But paragraph 9 of Rule 44 provides:

> No Member, officer, or employee of the Senate shall knowingly use his official position to introduce, request, or otherwise aid the progress or passage of congressionally directed spending items, limited tax benefits, or limited tariff benefits a principal purpose of which is to further only his pecuniary interest, only the pecuniary interest of his immediate family, or only the pecuniary interest of a limited class of persons or enterprises, when he or his immediate family, or enterprises controlled by them, are members of the affected class.[222]

The effect of paragraph 9 on paragraph 6 is not entirely clear. The "no pecuniary interest" certification requirement in Senate Rule 44(6) may, on one hand, be read to encompass only those earmarks that satisfy both a "principal purpose" test and a "limited class" test. As such, the Senate's "special" rule for earmarks would merely reflect the general prohibition that already exists under Senate Rule 37(4).[223] On the other hand, the Senate may construe Rule 44(6)'s certification requirement without any such qualification from paragraph 9. And in that event, as in the House, a lawmaker with $50,000 of stock in DD Corp. would be foreclosed from requesting any earmark directed at DD Corp., notwithstanding his or her motivation.

C. *Lawmakers as Investors*

Except in the special case of earmarks (which are political hot potatoes, in their own right), the nearly forty-year-old view that financial conflicts are best deterred by public disclosure and the

---

221. SENATE RULES, *supra* note 92 at 175, para. 6 (emphasis added) (Rule 44).
222. *Id.* para. 9 (Rule 44).
223. *See supra* note 143 and accompanying text.

discipline of the electoral process continues to dictate the ethical norms in Congress. Although all federal officials owe duties of trust and loyalty to the public, only congressional officials are left almost entirely on their own to decide for themselves what financial interests might be inconsistent with those duties.

But much has changed since 1977, when Congress last accorded the financial conflict issue extensive scrutiny. Among other changes, recent years have shown a much higher rate of personal wealth in Congress, substantially higher percentages of stock ownership among lawmakers, much more federal intervention in the economy and operations of private-sector businesses, and a heightened public awareness that lawmakers routinely profit from securities investments that intersect with their legislative activities.[224]

Most lawmakers in Congress are very wealthy, and the number of millionaires continues to rise.[225] Public disclosure forms filed for 2010 revealed that 250 lawmakers had an estimated net worth of more than $1 million: 183 of 435 Representatives (42%) and 67 of 100 Senators (67%).[226] These figures, however, substantially understate net worth because they do not reflect the value of personal or secondary residences that are not incoming producing and the EIGA's disclosure instructions allow investments and other assets to be reported in dollar amount ranges. Less than twenty years ago, 51 Representatives (12%) and 26 Senators were millionaires (26%).[227]

Stock ownership by members of Congress has also soared over the last several decades.[228] Academic researchers in one often-cited study examined disclosure reports from 650 members who served in the Senate and House between 2004 and 2008. They found that "422 [65%] reported holding a stock listed on the NYSE, NASDAQ or

224. Robert O'Harrow Jr. et al., *Rise in Stock Ownership Among Lawmakers Brings Ethics Concerns*, *WP Politics*, WASH. POST (Nov. 23, 2009), http://www.washingtonpost.com/politics/rise-in-stock-ownership-among-lawmakers-brings-ethics-concerns/2012/01/28/gIQArB2UYQ_story.html.

225. *See* Stephanie Condon, *Wealth in Congress Climbed as Others Saw Net Worth Stay Stagnant, Reports Show*, CBSNEWS (Dec. 27, 2011, 12:57 PM), http://www.cbsnews.com/8301-503544_162-57348729-503544/wealth-in-congress-climbed-as-others-saw-net-worth-stay-stagnant-reports-show/ ("[T]he net worth of lawmakers on Capitol Hill has jumped considerably in recent decades.").

226. Michael Beckel, *Most Members of Congress Enjoy Robust Financial Status, Despite Nation's Sluggish Economic Recovery*, OPENSECRETS.ORG (Nov. 15, 2011, 10:30 AM), http://www.opensecrets.org/news/2011/11/congress-enjoys-robust-financial-status.html.

227. Craig Winneker & Jonathan Ringel, *The Roll Call Fifty*, ROLL CALL, Jan. 20, 1992.

228. *See* O'Harrow et al., *supra* note 5.

AMEX at some point during that period."[229] To be sure, many lawmakers currently have investment portfolios comprised mostly of shares in diversified mutual funds and/or government securities, including U.S. treasuries and municipal bonds.[230] A far smaller percentage of lawmakers hold their assets in qualified blind trusts—fewer than twenty lawmakers reported such trusts in 2010.[231]

In addition to the sharp rise in stock ownership by lawmakers, recent years have brought congressional intervention in private sector businesses at unprecedented levels, with trillions of taxpayer dollars allocated for bank and auto company bailouts, health care reform, and economic stimulus projects.[232] Legislative decisions thus have a much greater likelihood of affecting the economic bottom line of publicly traded corporations—triggering direct and foreseeable impacts on the value of stock holdings in lawmakers' portfolios.

---

229. Andrew Eggers & Jens Hainmueller, *Capitol Losses: The Mediocre Performance of Congressional Stock Portfolios*, 75 J. POL. 535, 541 (2013).

230. *See* O'Harrow et al., *supra* note 5, at A1, A4; Brody Mullins et al., *Stock Law Leaves Congress Leeway*, WALL ST. J., June 15, 2013, at A7 (reporting that in 2012, "[s]everal members of Congress moved to shield themselves from criticism by selling individual stocks and shifting to mutual funds"); *see also* Paul Kane & Carol D. Leonnig, *Lawmakers Invested in Bailed-Out Firms*, WASH. POST, June 11, 2009, at A4, *available at* http://articles.washingtonpost.com/2009-06-11/politics/36861221_1_lawmakers-stock-holdings-disclosure (observing that then-Representative Barney Frank (D-Mass) "does not invest directly in stocks, instead concentrating largely on state and local bonds, with a small amount directed into mutual funds" and quoting Frank's statement that "I get a steady 4.5 percent, and I help my state in the process. I'm a patriot, and I'm making money, too.").

231. *See* Anne VanderMey, *Who Needs a Blind Trust?*, CNNMONEY (Oct. 22, 2012, 12:55 PM), http://finance.fortune.cnn.com/2012/10/22/blind-trust-mitt-romney/ (reporting that seven senators and twelve representatives had qualified blind trusts in place in 2010). Blind trusts serve to mitigate conflicts by removing the owner's control over the particular assets held by the trust. *See* JACK MASKELL, CONG. RESEARCH SERV., RS21656, THE USE OF BLIND TRUSTS BY FEDERAL OFFICIALS 1 (2005) (stating that "the use of a 'blind trust' is one of several methods of conflict of interest avoidance under federal law and regulation"); NYCBA 1970 REPORT, *supra* note 16, at 62–63 (endorsing the blind trust method of conflict avoidance and observing that "[w]hile not a full divestment of the assets involved, appropriate provision in the trust instrument can advance the desired independence of official decision-making"). *But see* Megan J. Ballard, *The Shortsightedness of Blind Trusts*, 56 U. KAN. L. REV. 43, 71 (2007) (suggesting changes to the EIGA and congressional rules that would "strengthen compliance, improve the way a trustee's performance is monitored, and enhance the independence of a trustee").

232. *See* O'Harrow et al., *supra* note 5, at A4; *cf.* Stephen M. Bainbridge, *Insider Trading Inside the Beltway*, 36 J. CORP. L. 281, 299 (2011) (observing that "the massive increase in federal involvement in financial markets and corporate governance as a result of the financial crisis of 2008 has made [insider trading] opportunities . . . even more widely available to government officials").

Possible connections between the stock investments of a particular lawmaker and his or her legislative actions can be drawn fairly easily. For almost a decade, the Center for Responsive Politics ("CRP"), a nonprofit research group, has been transcribing the annual paper disclosure reports filed by lawmakers and providing that data on its website (www.opensecrets.org). A few clicks on a computer mouse can produce a list of the "most popular congressional investments," which in turn reveals not only the top fifty publicly traded corporations in which lawmakers are most heavily invested but also a specific value range of the investments for each identified lawmaker.[233] Journalists, particularly the authors of the *Washington Post*'s "Capitol Assets" series, have made full use of the CRP's data, systemically comparing particular lawmakers' stock investments with their legislative activity.[234] The *Washington Post* has supplemented this extensive series of reports with an interactive database that allows users to (literally) connect the dots between congressional committee service and a lawmaker's stock investments.[235]

Among other findings, these reports in the *Washington Post* reveal that

- between the years 2007 and 2010, 130 lawmakers or their families traded stock—totaling between $85 million and $218 million—in 323 companies registered to lobby on bills that came before their committees;[236]
- roughly in that same time period, 73 lawmakers either "sponsored or co-sponsored legislation . . . that could benefit businesses or industries in which either they or their families are involved or invested;"[237]
- nearly 30 key lawmakers—with health-industry stock holdings totaling between $11 million and $27 million—helped draft landmark health-care

233. *See generally Most Popular Congressional Investments, 2011*, OPENSECRETS.ORG, http://www.opensecrets.org/pfds/overview.php?type=P&year=2011 (last visited June 26, 2013) (indicating "the most common assets among all members of Congress who served during all or part of 2011, ranked by the number of members invested in them, with breakdowns by party").

234. *See generally supra* note 5 (citing seven front-page news articles).

235. *See generally Capitol Assets: A Close-Up Look at Congressional Wealth*, WASH. POST, http://www.washingtonpost.com/blogs/gallery/capitol-assets/ (last visited June 26, 2013); *A Close-Up Look at Congressional Wealth*, WASH. POST, http://www.washingtonpost.com/wp-srv/special/capitol-assets/congressional-wealth-risk-matrix/ (last visited June 26, 2013) (revealing how the 535 Members of Congress position their investment portfolios and their wins (and losses) on Wall Street).

236. Keating et al., *supra* note 5.

237. Kindy et al., *supra* note 5, at A11.

legislation,[238] and "[i]n the medical-device field alone, 108 lawmakers collectively own between $6 million and $14 million worth of stock;"[239]

- during the financial crisis, at least 18 of the 60 members of the House Financial Services Committee held stock in firms that received federal bailout assistance;[240]
- between 2004 and 2009, 19 of the 28 senators on the Senate Armed Services Committee held assets—totaling between $3.8 million and $10.2 million—in companies under contract with the Pentagon;[241] and
- many House and Senate committees have memberships with "disproportionately large holdings in companies or industries they oversee . . . ."[242]

Although the composite picture falls short of proving that lawmakers place their personal financial interests ahead of the public they serve, a large segment of the public has apparently taken away that disturbing message.[243] And because anticonflict measures are "more concerned with what might have happened in a given situation then what actually happened,"[244] the public perception is the very problem that requires the cure.

The *Washington Post*'s "Capitol Assets" series also reveals important insights about lawmakers and their own views about the overlap between their stock investments and their legislative activity.[245] Indeed, the lawmakers who were contacted in connection

---

238. Kane, *supra* note 5.

239. O'Harrow et al., *supra* note 5, at A6.

240. Kane & Leonnig, *supra* note 230.

241. Higham et al., *supra* note 5, at A2; *see also Conflicting Standards*, WASH. POST, http://www.washingtonpost.com/wp-srv/special/politics/conflicting-senate-standards/ (last visited June 26, 2013).

242. O'Harrow & Keating, *supra* note 5 at A6 (reporting, among other examples, that: House Transportation and Infrastructure Committee members "as a group owned almost six times more holdings in transportation firms"; House Energy and Commerce Committee members had "heavier than average investments in companies such as Oracle, Nokia, AT&T and Verizon"; senators on the Environment and Public Works Committee "had almost three times the value of agribusiness holdings as their colleagues on other committees"; and senators on the Banking, Housing and Urban Affairs Committee "had on average almost twice the value of holdings in finance, insurance and real estate as that chamber as a whole").

243. *See infra* notes 256–62 and accompanying text (quoting observations by several lawmakers).

244. United States v. Miss. Valley Generating Co., 364 U.S. 520, 550 (1961).

245. *See* David S. Fallis et al., *Congressional Earmarks Sometimes Used to Fund Projects Near Lawmakers' Properties*, WASH. POST, Feb. 7, 2012, at A1, *available at* http://www.washingtonpost.com/investigations/congressional

with many of the reports frequently emphasized their full compliance with the Senate or House rules on financial investments as well as with the public disclosure provisions of the EIGA.[246] For example, when nineteen senators on the Senate Armed Services Committee were asked to comment on the propriety of their individual stock holdings in defense contractors, nearly a dozen of them responded through a spokesperson that he or she has always strictly adhered to all Senate rules about financial investments and fully disclosed all such investments.[247]

Lawmakers' views of their own investment decisions have prompted others to question whether the traditional means for deterring lawmakers' financial conflicts—public disclosure coupled with the electoral process—could actually be exacerbating the risk of self-interested legislative activity. Indeed, research in the field of behavioral economics shows that "[o]nce people disclose a potential conflict . . . they often feel morally absolved—which can blind them to the possibility that they may still be biased."[248] Moreover, because "'[p]eople can be biased by surprisingly small incentives,. . . even . . . a congressman's [modest] portfolio . . . could still influence his behavior in votes and hearings.'"[249]

Given lawmakers' status as fiduciaries and the accumulated knowledge about lawmakers as stock market investors, what explains the fact that nearly forty-year-old decisions continue to dictate current congressional norms with respect to financial conflicts of interest?

Apart from concerns about insulating lawmakers from the interests of their constituents,[250] the other primary concern is that a divestment rule would alter incentives to serve in Congress. Although some have argued that a divestiture requirement could jeopardize our nation's ability to attract and retain talented politicians and staffers to Congress,[251] it is also possible that an

---

-earmarks-sometimes-used-to-fund-projects-near-lawmakers-properties/2012/01/12/gIQA97HGvQ_story.html.

246. *See Conflicting Standards*, *supra* note 241 (showing responses from senators).

247. *See* Higham et al., *supra* note 5, at A2; *see also Conflicting Standards*, *supra* note 241 (hyperlinking verbatim text of the spokespersons' responses).

248. *See* Jason Zweig, *A Perk of Power: Trading in Companies You Oversee*, WALL ST. J., Apr. 10, 2010, at B10, *available at* http://online.wsj.com/article/SB10001424052702304703104575174124009720464.html (citing Professor George Loewenstein, a behavioral economist at Carnegie Melon).

249. *Id.*

250. *See supra* text accompanying note 191.

251. *See* Higham et al., *supra* note 5, at A2 (reporting the view by congressional experts that divestiture rules "would deter good candidates for office"). In 1961, the Senate Armed Services Committee discussed the possibility of extending its defense contractor divestiture rule for senior

even greater number of persons may be drawn to serve in an institution that has opted to take fiduciary principles more seriously.[252] The question, of course, is an empirical one. But modern portfolio theory instructs that most investors who hold stocks and bonds in individual companies will not be able to achieve benchmark-beating returns.[253] Although at one time researchers suggested that congressional officials had investment portfolios that substantially outperformed the overall stock market,[254] a more recent study indicates otherwise, finding that the average lawmaker underperformed the market by between 2% and 3% annually.[255] Ironically, then, a precommitment strategy that would tie lawmakers to the mast of passive index funds could actually increase lawmakers' aggregate wealth. With a stock divestiture requirement in place for ten years, we might actually see even greater numbers of millionaires in Congress.

IV. ACHIEVING GREATER PARITY

As the foregoing reveals, the anticonflict rules that govern Congress's members and employees are substantially less restrictive than the statutes and rules that apply to federal officials in the executive and judicial branches. Legislation (or Senate and House rules) limiting the type of securities that congressional officials may own would be an important first step toward greater parity. Because lawmakers are expected to work and vote on a multitude of issues that impact particular industries and often specific companies, the rigid recusal requirements that govern executive branch officials and judges are neither workable nor appropriate as

---

Department of Defense officials to its own committee members. Although several senators spoke in favor of changing the double standard, other senators expressed opposition. Then-Senator Prescott Bush (R-Conn.) contended: "When you pass a law like that, you will have the greatest mass resignation that the world has ever seen . . . For heaven's sake, if you want to bring together a lot of people that do not have any touch with reality in this country to make the laws, God help the United States, in my judgment." *Id.* (quoting hearing transcript). The question was never called to a vote. *Id.*

252. Congress could ease the financial burden on legislative branch officials by amending the tax code to allow for the deferral of any capital gains that result from securities sales that were subject to a divestiture rule. *See supra* text accompanying note 95.

253. *See generally* BURTON G. MALKIEL, A RANDOM WALK DOWN WALL STREET: THE TIME-TESTED STRATEGY FOR SUCCESSFUL INVESTING 195–214 (10th ed. 2012).

254. Alan J. Ziobrowski et al., *Abnormal Returns from the Common Stock Investments of Members of the U.S. House of Representatives*, 13 BUS. & POL. 1, 1 (2011); Alan J. Ziobrowski et al., *Abnormal Returns from the Common Stock Investments of the U.S. Senate*, 39 J. FIN. & QUANTITATIVE ANALYSIS 661, 669 (2004).

255. *See* Eggers & Hainmueller, *supra* note 229, at 536.

a standard solution for lawmakers. Rules requiring securities divestment, on the other hand, would be both workable and appropriate. Indeed, federal agency officials often operate under strict divestiture requirements that are expressly designed to thwart public perceptions of personal financial gain from agency actions, programs, or policies.

A. Additional Reasons for Change

There are several reasons why the timing is particularly apt for conflicts-of-interest reform in the legislative branch that would begin with limitations on securities investments. First and foremost, a divestiture requirement would combat the troubling perception that congressional officials can—and routinely do—place their own financial well-being ahead of the best interests of the public they serve. Although lawmakers clearly take issue with that perception's accuracy, they have been candid in acknowledging its widespread persistence. Indeed, lawmakers know all too well that "Americans rate Members of Congress at or near the bottom of the list when it comes to perceived honesty and ethical standards;"[256] that "[m]ost Americans think that everything done in the financial crisis was done to help specific institutions and specific people;"[257] and that there is "a sense that elites in Washington are using their positions to get ahead financially."[258] Lawmakers likewise appreciate that "the public opinion of Congress [is] so bad . . . because Congress has been so bad,"[259] that "there is a breakdown of trust,"[260] and that "the American people . . . deserve the right to know that their lawmakers' only interest is in what is best for the country, not what is best for their own financial interests."[261] As Senator Joseph Lieberman emphasized at the start of the Senate Hearing on the STOCK Act, if the "law seems to allow Members of Congress to take advantage of their public position for personal gain, the trust that needs to exist between the American people and our government will be further eroded."[262]

---

256. *Senate STOCK Act Hearing*, *supra* note 183, at 3 (statement of Ranking Member Susan Collins).

257. *House STOCK Act Hearing*, *supra* note 119, at 6 (statement of Rep. Bradley Miller).

258. 158 CONG. REC. S241 (daily ed. Feb.1, 2012) (statement of Sen. Sherrod Brown).

259. 158 CONG. REC. S148 (daily ed. Jan. 30, 2012) (statement of Sen. Joseph Lieberman).

260. *Senate STOCK Act Hearing*, *supra* note 183, at 6 (testimony by Sen. Scott Brown).

261. *Id.* at 5 (testimony by Sen. Kirsten Gillibrand).

262. *Id.* at 1 (opening statement of Chairman Joseph Lieberman). *See also* Frank Newport, *Congress Begins 2013 with 14% Approval*, *Politics*, GALLUP (Jan. 11, 2013), http://www.gallup.com/poll/159812/congress-begins-

Legislative branch reforms that would place limitations on securities ownership would also save countless hours of government time. Some of this time involves work by the members and staffers on the Standards and Ethics Committees in the Senate and House, who respond each year to literally thousands of requests from lawmakers seeking legal advice on a range of activities, "including their work on legislation that might pose a conflict."[263] Moreover, in the wake of the STOCK Act, individual members and senior staff must now file transaction reports within forty-five days of a securities purchase or sale.[264] These reports are likely being reviewed by the staff of the Securities and Exchange Commission, if not regularly, at least sporadically. Far fewer advisory ethics opinions would need to be rendered and far fewer transaction forms would need to be filed and reviewed if members and employees of Congress were generally prohibited from owning any securities other than government securities or shares in diversified mutual funds.

Even more important than the time savings, legislative branch reform would substantially facilitate compliance with the STOCK Act's substantive restrictions. Although the insider trading prohibitions arising under the federal securities laws extend only to actions with "corrupt intent,"[265] an anticonflict restraint that essentially prohibits stock trading outright would be an important guard against inadvertent trading while in possession of material nonpublic government information. Lawmakers and staffers have access to a wide array of material nonpublic information pertaining to specific industries and the general economy, and managing to avoid trading while aware of such information is a difficult endeavor.[266] Indeed, a lawmaker who sells stock in a company

---

2013-approval.aspx (reporting that the 2012's yearly average of 15% was "the lowest in Gallup's 38-year history of asking" the [approval/disapproval] question). For a student note highlighting Congress's image problem, see generally Paul D. Brachman, Note, *Outlawing Honest Graft*, 16 N.Y.U. J. LEGIS. & PUB. POL'Y 261 (2013).

263. *See* Kindy et al., *supra* note 5 (reporting that between 2007 and 2011, "lawyers for the two committees issued at least 2,800 written opinions to lawmakers, sent 6,500 e-mails containing advice and provided guidance over the phone 40,000 times, according to records kept by the two committees").

264. *See* MASKELL, *supra* note 61, at 1 ("The act . . . requires public reporting within 30 days of receipt of a notice of a covered financial transaction (but in no event more than 45 days after such [a] transaction.").

265. *House STOCK Act Hearing*, *supra* note 119, at 32, 40–41 (statement of Robert Khuzami, Director, SEC Division of Enforcement).

266. For news reports raising questions about suspiciously timed securities trading, see, e.g., Kimberly Kindy et al., *Lawmakers Reworked Financial Portfolios After Talks with Fed, Treasury Officials*, WASH. POST, June 25, 2012, at A7 (reporting that at least "34 members of Congress recast their financial portfolios following phone calls or meetings with high-ranking Treasury

precisely to avoid the appearance of self-interested decision making could actually be creating a problem for herself under federal insider trading law if she were aware of material nonpublic information at the time of that sale.[267]

Limitations on the ownership of stock in individual companies would likewise bolster the STOCK Act's initial public offering ("IPO") provision, which prohibits federal officials from purchasing securities in an IPO "in any manner other than is available to members of the public generally."[268] Because the investor demand for shares in an IPO usually exceeds the supply, underwriter allocations often preference institutional investors and wealthy individual investors with connections to Wall Street.[269] Distinguishing between the typical allocation process and illegal preferential treatment extended to lawmakers will be quite a challenge, to say the least.

Finally, heightened restrictions on lawmakers' securities holdings could pave the way for further conflict-of-interest reform in connection with other financial investments. Standards and ethics committees in the House and the Senate might, for example, be more inclined to forsake longstanding interpretations of existing rules by issuing new guidance that would recommend conflict avoidance relating to other types of investments. New limitations on securities ownership could also spark additional rulemaking efforts. For instance, the "no financial interest" certification now required to accompany a lawmaker's earmark request could be expanded to encompass anticipated property appreciation if the location of a proposed public works project is next to or within a few miles of residential, commercial, or investment property owned by the lawmaker or a spouse.[270]

Department and Federal Reserve officials during the economic crisis"); Brody Mullins et al., *Congress Staffers Gain from Trading in Stocks*, WALL ST. J., Oct. 11, 2010, at A1 (reporting the newspaper's "analysis of more than 3,000 disclosure forms covering trading activity by Capitol Hill staffers for 2008 and 2009").

267. *See* Nagy, *supra* note 128, at 1129 (discussing the "awareness" standard set out in SEC Rule 10b5-1).

268. STOCK Act, Pub. L. No. 112-105, § 12, 126 Stat. 291, 300 (2012) (codified at 15 U.S.C. § 78u-1(i)).

269. *See* Stephen Gandel, *The IPO Market's Hottest Craze: Dividends, Term Sheet*, CNNMONEY (Apr. 15, 2013, 6:00 AM), http://finance.fortune.cnn.com/2013/04/15/ipos-dividends/ (explaining investor demand for IPO dividend stocks); OFF. INVESTOR EDUC. & ADVOCACY, SEC, SEC Pub. No. 133, INVESTING IN AN IPO 2 (2013), *available at* http://www.sec.gov/investor/alerts/ipo-investorbulletin.pdf ("underwriters . . . will distribute most of the shares in the IPO to their institutional and high net-worth clients").

270. *See* David S. Fallis et al., *Congressional Earmarks Sometimes Used to Fund Projects Near Lawmakers' Properties*, WASH. POST., Feb. 6, 2012, at A1, *available at* http://articles.washingtonpost.com/2012-02-06/politics/35442262_1

B. Specific Proposals

As reflected in the rare bipartisan momentum that fueled the STOCK Act's passage (by near unanimous votes of 96-3 in the Senate and 417-2 in the House),[271] congressional ethics reform is a legislative priority around which liberals, moderates, and conservatives can and should unite. It is also a priority strongly supported by President Obama, who has urged Congress on at least two occasions to "limit any elected official from owning stocks in industries that they have the power to impact."[272] The subsections that follow set forth two specific proposals for limiting the securities investments that may be held by members and employees during their public service in Congress.

1. Investment Limitations Based on Committee Service

As a "Congress of committees, not individuals,"[273] financial conflicts-of-interest reform should begin with investment limitations tied to a lawmaker's committee membership. Although Congress chose not to travel down this path when the NYCBA proposed it in 1970, today's lawmakers may be more amenable to change in light of the groundwork already laid by the STOCK Act and the additional empirical evidence now available regarding the investment practices of Congress's members.[274]

In the course of its three-year study of the legislative branch, the NYCBA's Special Committee on Congressional Ethics interviewed 120 Senators and Representatives.[275] The interviews and other data convinced the Committee that "the typical Member of

---

_congressional-earmarks-congressional-knowledge-stock-act (reporting that, since 2008, thirty-three lawmakers "have directed more than $300 million in earmarks and other spending provisions to dozens of public projects that are next to or within about two miles of the lawmakers' own property"). According to the *Post*, the lawmakers were able to certify that they (together with spouses) lacked a "financial interest" in the earmarks because, in general, the increases in the value of the properties were regarded as "incremental and indirect" and were experienced "as a member of a class of landowners in the vicinity" of the public works project. *See id.* (quoting House Ethics Committee advisory opinion issued to lawmaker who sought an earmark to build a bus terminal and park-and-ride center near seven commercial properties he owned).

271. *See* Robert Pear, *Insider Trading Bill Clears Congress*, N.Y. TIMES, Mar. 23, 2012, at A13, *available at* http://www.nytimes.com/2012/03/23/us/politics/insider-trading-ban-for-lawmakers-clears-congress.html?_r=0.

272. *See* President Barack Obama, Remarks on Signing the Stop Trading on Congressional Knowledge Act 2012, *in* DAILY COMP. PRES. DOCS. 247 (April 4, 2012), *available at* http://www.gpo.gov/fdsys/pkg/DCPD-201200247/content-detail.html; *see also* President Barack Obama, *supra* note 11.

273. NYCBA 1970 REPORT, *supra* note 16, at 69.

274. *See supra* notes 235–42 and accompanying text (detailing investigative findings by the *Washington Post*).

275. NYCBA 1970 REPORT, *supra* note 16, at xxv.

Congress has financial interests with some potential for clouding his independence of judgment on legislation,"[276] and that most of these conflicts were "avoidable" because they were neither inherent (they did not involve a status such as a homeowner, parent, or veteran), politically dictated (they did not involve, for example, a "farmer elected from an agricultural district"), nor personally necessary (they did not involve "small, closely held family enterprises").[277] The Committee's basic thesis was "that an avoidable conflict of interest should normally be avoided [and] . . . if not avoided, it should be disclosed to the Member's colleagues and to the public and perhaps should result in disqualification from voting or committee service."[278]

The Committee grounded its strong preference for "interest avoidance by selective investment" in the fiduciary duty of loyalty.[279] After emphasizing the risk of impaired judgment that arises whenever there is a temptation to serve personal interests, the Committee opined:

> The quality of specific results is immaterial. . . . Like other fiduciaries, such as guardians, executors, lawyers, and agents, the public trustee has a duty to avoid private interests which cause even a risk that he will not be motivated solely by the interests of the beneficiaries of his trust. Properly conceived, conflict-of-interest regulation does not condemn bad actions so much as it erects a system designed to protect a decision-making process. It is preventive and prophylactic. Its aim is not detection and punishment of evil, but providing safeguards which lessen the risk of the undesirable action.[280]

The Committee further observed that "[t]he fiduciary concept makes it unnecessary for our recommendations to be supported by evidence that identifiable harm to the public has resulted" from such avoidable financial conflicts.[281]

Along with its general thesis of interest avoidance, the Committee advanced several specific recommendations. These included:

> **Recommendation 2B** – Each Member of Congress should make every reasonable effort to utilize available investment alternatives which minimize instances in which it may appear

276. *Id.* at 51.
277. *Id.* at 44–46.
278. *Id.* at 47.
279. *See id.* at 61–63.
280. *Id.* at 39.
281. *Id.* at 52.

> that his official decisions may be influenced by personal economic interests.[282]
>
> **Recommendation 2D** – Each house should adopt the following rule: "When a Member is appointed to a committee, he should, if reasonably possible, avoid all economic interests which may be specifically affected by legislation within the jurisdiction of his committee."[283]
>
> **Recommendation 2E** – Each house of Congress should adopt the following rule: "It shall be the duty of each committee to establish rules governing financial interests of its members and employees in matters coming before the committee."[284]

To be sure, the NYCBA's general thesis and specific "interest avoidance" recommendations both influenced and impacted some of Congress's members and employees. Indeed, although it is difficult to measure with any precision, it is quite likely that many lawmakers and staffers took Recommendation 2B to heart; many lawmakers have investment portfolios that avoid corporate stocks altogether and others have placed their securities holdings into qualified blind trusts.[285] In addition, Recommendation 2D found its way in the committee staff divestment rule that is now set out in Senate Rule 37(7).[286]

Yet overall, the vast majority of lawmakers have pretty much eschewed "interest avoidance" as a principal method for controlling financial conflicts, at least with respect to stock investments in individual companies.[287] But, even more avoidable and all the more troubling are those securities investments in companies within an industry over which a lawmaker's committee has jurisdiction.[288] Here the parallels between committee members and executive branch officials are striking: lawmakers on committees such as Armed Services, Banking, Financial Services, and Telecommunications are wrestling with the very same policy issues confronting the officials at the Pentagon, Treasury, SEC, and FCC. Greater parity could be achieved with a federal statute (or new House and Senate rules) that would restrict members and their senior staffs from owning securities in companies with business that

282. *Id.* at 63.
283. *Id.* at 68.
284. *Id.* at 71.
285. *See supra* notes 230–31 and accompanying text.
286. *See supra* note 159 and accompanying text.
287. *See supra* notes 228–29 and accompanying text.
288. *See* O'Harrow Jr. & Keating, *supra* note 5 (observing that lawmakers "try to get on the committees in which they have a vested interest," which places them "in a better position of influencing the performance of their investments . . . or at least appearing to have that ability" (quoting Steve Ellis, vice president of Taxpayers for Common Sense)).

is directly and foreseeably affected by the work of any committee on which the lawmaker holds membership.

2. *Investment Limitations Applied More Broadly*

In early 2012, as the STOCK Act bill was headed toward passage in the Senate, nearly two-dozen senators sought to build on the bill's core insider trading and transaction reporting provisions.[289] The result was a bevy of proposed "good-government" amendments.[290] Expressing his concern that the bill's chances for passage were being jeopardized, Senator Lieberman invoked a Dr. Seuss metaphor: "We don't want this bill, which does so many important things, to be so loaded up that it falls by the wayside like Thidwick's antlers."[291] To prevent that from happening, the Senate passed an order providing for an up-or-down vote on most of the proposed amendments, but requiring a sixty-vote threshold and limiting debate to two minutes equally divided between those members in favor and those opposed.[292]

In the course of the Senate's consideration of the twenty-two amendments that were then pending on the STOCK Act bill,[293] Senators Sherrod Brown (D-OH) and Jeff Merkley (D-OR) advanced a proposal that would have placed a broad limitation on securities investments by members and certain employees of the Senate.[294]

---

289. *See* 158 CONG. REC. S1979 (daily ed. Mar. 22, 2012) (statement of Sen. Joseph Lieberman) (noting that the legislation being sent to the President contained "several provisions that were added in the Senate or House to strengthen the bill").

290. *See* 158 CONG. REC. S1980 (daily ed. Mar. 22, 2012) (statement of Sen. Joseph Lieberman) (noting that there had been twenty amendments to the STOCK Act). Most of the proposed amendments, however, were voted down, including Toomey amendment No. 1472 to permanently ban earmarks; Paul amendment No. 1490 to require former lawmakers to forfeit federal retirement benefits if they work as a lobbyist or engage in lobbying activities; and DeMint amendment No. 1488 to express the sense of the Senate for a joint resolution proposing an amendment to the Constitution that would impose term limitations on lawmakers. *See* 158 CONG. REC. S290–310 (daily ed. Feb. 2, 2012).

291. 158 CONG. REC. S148 (daily ed. Jan. 30, 2012) (statement of Sen. Joseph Lieberman). As Senator Lieberman recounted, *Thidwick the Big-Hearted Moose* told the story of animals in a forest who were warmly welcomed to take up residence in a moose's antlers "until finally there is too much there and his antlers fall off and they all fall to the ground." *Id.*

292. 158 CONG. REC. S290 (daily ed. Feb. 2, 2012) (statement of Sen. Harry Reid).

293. *See id.* at S290–91 (listing pending amendments).

294. *Id.* at S309 (statement of Sen. Sherrod Brown). Nearly twenty years ago, similar legislation mandating divestiture had been proposed in the House. *See* 141 CONG. REC. E731–01 (Mar. 29, 1995) (statement by Rep. Bernie Sanders introducing H.R. 1356, "The Public Interest Legislation Act"). The bill, which had five cosponsors, would have amended the EIGA to require lawmakers to

Their amendment was termed the "Putting the People's Interests First Act of 2012," and Senator Brown's advocacy was necessarily brief:

> Mr. President, the amendment Senator Merkley and I have proposed would require all Senators and their senior staff to sell individual stocks that create conflicts or to place their investments in blind trusts. You can still invest in broad-based mutual funds. You can keep your ownership interest in your family farm or small business.
>
> If you are setting up a blind trust, you can instruct the trustee to hold on to your stock in your family company.
>
> Current Senate ethics rules require committee staff making more than $25,000 a year to "divest [themselves] of any substantial holdings which may be directly affected by the actions of the committee for which [they work]."
>
> All Senate Merkley and I are saying is, Members of the Senate should hold ourselves to the same standard we already require of our committee staff and executive branch employees.
>
> As Senator Merkley said, baseball players cannot bet on their games. We should not be able to hold stock in individual companies and then vote on issues that affect our holdings.[295]

Two members spoke in opposition. Senator Pat Toomey (R-Penn.) disagreed with the "fundamental premise of this amendment."[296] He also expressed a specific concern with the amendment's reach, stating:

> I read the definition of the securities that would be covered and as the securities attorneys have advised us on this—we would be required to divest ourselves even of our investment in a small family-owned business, a business that, perhaps, has absolutely no market whatsoever for the equity, and we would, nevertheless, be forced to sell that where there is no buyer.
>
> I think that is a very unreasonable standard, so I would urge a "no" vote on this amendment.[297]

The second opponent was Senator Lieberman, who expressed the view that a new divestment requirement would be unnecessary in

---

divest themselves of any asset or interest which exceed $1,000 in real property (other than a personal residence) or in any form of securities, or place such assets in a qualified blind trust. *Id.*

295. *Id.* at S295, S309 (statement of Sen. Sherrod Brown) (alterations in original).

296. *Id.* at S309 (statement of Sen. Pat Toomey).

297. *Id.*

light of the STOCK Act's requirement for prompt (no later than forty-five days) reporting of securities purchases and sales:

> This amendment would take Congress from where we have always been and are going to be after this law passes. In pursuit of disclosure and transparency, sunshine is the best guarantee of integrity. This would be the first time I am aware of that in the legislative branch we would require divestment of personal holdings. For that reason, I oppose the amendment.
>
> Remember, in the underlying bill we have increased the public's access to information about our holdings and our transactions. Ultimately, that knowledge ought to be enough to guarantee the public or to energize the public to make sure we are following the highest ethical norms. Divestment, in my opinion, is a step too far.[298]

The proposed "Putting People First Act" was defeated by a Senate vote of 26-73.[299] But that loss should not seal the proposal's fate. Although its details and definitions could be refined after additional consideration, the proposed legislation's general prohibition had a commendable simplicity:

> A covered person shall be prohibited from holding and shall divest themselves of any covered investment that is directly, reasonably, and foreseeably affected by the official actions of such covered person, to avoid any conflict of interest, or the appearance thereof. Any divestiture shall occur within a reasonable period of time.[300]

The term "covered person" included members and senior staff of the Senate (whose annual base pay exceeded $120,000) as well as their spouses and dependents.[301] And the term "covered investment" was defined expansively to mean "investment in securities in any company, any comparable economic interest acquired through synthetic means such as the use of derivatives, or short selling any publicly traded securities."[302] But the general prohibition applied neither to broad-based investments (such as shares in diversified mutual funds) nor to a spouse's investments in the securities of the company in which the spouse is employed. The proposed legislation also permitted the Senate Ethics Committee to authorize covered persons, "on a case-by-case basis," to place their securities holdings

298. *Id.* (statement of Sen. Joseph Lieberman).
299. 158 CONG. REC. S309 (daily ed. Feb. 2, 2012).
300. 158 CONG. REC. S243 (daily ed. Feb. 1, 2012).
301. *Id.*
302. *Id.*

in a qualified blind trust.[303] In the event of a covered person's violation of the general prohibition, the Senate Ethics Committee was required to notify the United States Attorney for the District of Columbia, and knowing violations could warrant a fine of no more than $50,000.[304]

A federal statute (or new House or Senate rules) along the lines proposed for the STOCK Act would be an effective reminder to Congress's members and employees that they serve in a fiduciary capacity. And while a prophylactic measure such as this would hardly solve every agency problem in politics, it would be a substantial step in the right direction.

CONCLUSION

Congress has long viewed its members' personal financial stake in legislative decisions as an extraneous factor that can—except in rare cases—be set aside for the good of the public. Yet federal law does not leave government officials in the other two branches completely to the nature of their better angels. Nor does state corporate law leave interested directors entirely on their own to wrestle away financial conflicts in the course of their business judgments. Although all fiduciaries are supposed to act solely for the benefit of their entrustors and never for the benefit of themselves, prophylactic rules are necessary to ensure that fiduciaries do, in fact, act loyally. Congress imposes stringent financial conflict-of-interest restraints on executive and judicial officers and employees, and it should regulate itself with a similar fidelity to fiduciary principles.

303. *See supra* note 231 (discussing qualified blind trusts).
304. 158 CONG. REC. S243 (daily ed. Feb. 1, 2012).

CATO INSTITUTE | Center for Monetary and Financial Alternatives

Examining Stock Trading Reforms for Congress
Questions for the Record to Jennifer J. Schulp
Submitted May 31, 2022

Questions from Committee Majority

1. **In your testimony, you acknowledged that "concerns have persisted about lawmaker stock trading," despite the passage of the STOCK Act. You testified that, in your view, measures such as "banning lawmakers from owning or trading stocks ... are too broad for preventing insider trading and too narrow to effectively address the question of financial conflicts of interest." You recommended that instead, "it is better to focus on increasing transparency through disclosure."**

   a. **What other specific suggestions do you have for reforming the existing disclosure requirements to improve transparency?**

As I outlined in my written testimony,[1] the first step is to ensure compliance with existing disclosure requirements. This likely requires some mix of better education for those subject to the requirements and a better mechanism for ensuring that those who do not comply with their responsibilities are subject to penalties.

With respect to penalties, the current penalty structure—even if consistently applied—is likely insufficient to deter noncompliance. First, the current penalty structure refers to money due for delinquent filings as a "late filing fee," which implies that filing periodic transaction fees in an untimely manner is simply a matter of paying the late fee, rather than non-compliance with statutorily required reporting. Any monetary consequence for untimely filing should be described as a penalty or sanction, not a late filing fee. Second, a penalty currently is initially triggered by a late-filed report. But because the disclosure relates to the transaction itself—not a report that may aggregate transactions—penalties should be tied at all points to the number of late-reported transactions, not the late-filed report. In other words, penalties should be imposed based on the number of late-reported transactions, not late-filed reports. Third, the level of the penalty—beginning at $200—is too low. Transactions that exceed $1000 are required to be reported, meaning that penalty reflects at most 20% of the value of the transaction. There are a number of ways to think about structuring a deterrent penalty structure, but it is worth considering whether a higher flat penalty (for example, $500 per transaction) or whether a percentage of the value of the transaction (for example, 30% or more) make sense. In order to ensure that late filings are made within a timely manner, it is

[1] Jennifer J. Schulp, Testimony before the Committee on House Administration, Hearing on "Examining Stock Trading Reforms for Congress" (April 7, 2022) at 5, https://docs.house.gov/meetings/HA/HA00/20220407/114485/HHRG-117-HA00-Wstate-SchulpJ-20220407.pdf.

worth considering whether those penalties should increase after a certain period of delinquency—for example, after more than a month of delinquency, the flat penalty or percentage penalty imposed would increase. Those who repeatedly fail to file timely periodic transaction reports should also be subject to higher penalties.

Additionally, periodic transaction reports that are filed in an untimely manner should be publicly identified as such when published. Ideally, this data should be presented in a form such that it would be easy for someone to determine whether any particular lawmaker has filed reports in an untimely fashion.

Additional transparency also can be achieved through shortening the timeframe for reporting transactions and by requiring periodic transaction reporting for diversified fund investments. Please see my answers to questions 2 and 5 below.

b. For items that must be disclosed now – such as certain assets, transactions, or liabilities – are there aspects of the way those items are currently reported that could be improved or additional detail that could be provided?

The ability to file periodic transaction reports on paper should be discontinued; these reports can be difficult to read when made available to the public and introduce a number of uncertainties into the reporting process, including the ability to provide information in a non-conforming manner and the need for rules about receipt of paper documents.

The public access system should also be redesigned to provide easy access to transaction information that can be sorted by lawmaker and by security. Given the difficulties of accessing the information provided, it is arguable that the spirit of the STOCK Act in requiring that information contained in the periodic transaction reports be available for the public to "search, sort, and download" the data is not being met.

c. Are the current reporting intervals by which filers indicate the value of reportable items sufficient to achieve the law's goals regarding disclosure and transparency?

The reporting bands for transactions tend to be relatively wide. While this makes sense to protect some privacy for lawmakers, it is worth revisiting whether those bands are serving their purposes. I do not have specific recommendations for revising the bands, but I'd suggest that the use of the bands be studied to determine whether all of the bands provide useful information. For example, several bands apply to very large transactions; is there a need for separate bands for very large transactions or should those be combined due to low usage? Conversely, if there is heavy usage of a particular band of transaction, it may be worthwhile to consider breaking those bands into smaller ranges to show more differentiation in reporting.

2. You testified, the "STOCK Act provides a good foundation for this transparency, but it has fallen short of its potential, and enhancements should be considered to provide additional transparency." One specific example you provided is "shortening the long lag between the execution of a trade and the deadline for disclosure," and you observed that

"corporate insiders are required to disclose within two days," although you also said that the example of corporate insiders "is not a completely comparable situation to Congress."

a. **With respect to requiring faster disclosure of transactions than the deadline currently established by the STOCK Act, what is a reasonable deadline?**

Because corporate insiders usually have more support in reporting than most Members of Congress can expect to, and because the purchase or sale of company stock by insiders can itself be a stock price moving event, very fast turnaround for reporting is more practical for insiders. Insiders usually have two business days to report transactions on Form 4.[2]

Even if a two-day reporting deadline is not practical for Members of Congress, the current long lag between the execution of a trade and the deadline for disclosure—30 days after the transaction or no more than 45 days after the trade if the lawmaker did not become aware of the trade when executed—contrasts sharply with insider reporting timetables. Moreover, lawmakers are given a 30-day grace period beyond those generous time periods before which their submission is determined to be non-compliant.

As an initial matter, no grace period should be applied for lawmakers who are given a month or more to report; the original time period for reporting is generous, especially when trades information is often easily accessible to lawmakers through online portals.

But even beyond the grace period, it is not unreasonable to expect Members to be more proactive in reporting transactions than waiting for a monthly statement. I suggest a week is an appropriate time frame for reporting, and there can be some consideration of an appropriate grace period if necessary. To ease this process, I'd suggest exploring the possibility of automation of the process; many private entities that impose trading restrictions on their employees use automated software to assist with collecting the trading information and with review of that information.

b. **If a shorter deadline is established, does it make sense to apply that deadline to transactions of significant amount, which exceed a particular threshold, or would it make more sense to subject all transactions – regardless of amount – to the same revised deadline?**

If a shorter deadline is established, it should apply to all transactions, regardless of amount.

3. **The hearing included discussion of the compliance costs associated with the creation and maintenance of a qualified blind trust and other impacts on filers. For example, Ranking Member Rodney Davis stated that he had been informed by a financial advisor that "most financial firms won't even take on a client for a blind trust unless they meet certain asset**

[2] *See* Securities and Exchange Commission, Insider Transactions and Forms 3, 4, and 5, available at https://www.sec.gov/files/forms-3-4-5.pdf.

holdings and activity requirements." You testified that, "Compliance costs for blind trusts tend to be substantial," and that it can take "multiple thousands of dollars to set one up."

a. **What is your understanding of the typical costs associated with establishing and maintaining a qualified blind trust? What is the typical range of costs for an attorney or other qualified professional to create such a trust? Once such a trust has been created, what is the typical range of annual costs for a trustee to administer the trust? For each, are these costs typically based on hourly or other similar basis, such as a percentage of the total assets managed in the trust?**

The cost of establishing a blind trust can vary, but my understanding is that it usually costs several thousand dollars to establish a trust, including the costs for an attorney to draft the trust agreement. The process of establishing the trust may also be complicated depending on how much must be done to transfer the assets to the trust.

Maintenance fees can also vary, but include compensation paid to the trustee and to an investment fiduciary (who may or may not be the same individual or entity). Those fees are usually based on a percentage of total assets managed in the trust, but again, the arrangement may vary. Those fees may also be in addition to the fees charged to manage the account (which the lawmaker may not have been previously incurring depending on how he or she was managing their assets prior to the blind trust).

b. **What is your understanding of how common it is for financial firms or advisors to set minimum criteria for an individual's financial assets or financial activity to either create or manage a blind trust?**

I do not have a firsthand understanding of how common it is for financial firms to set minimum criteria for maintaining a blind trust, although I would not be surprised if that were the case. Firms often maintain minimum criteria for advisory relationships with clients, irrespective of the existence of a blind trust, and it would not be surprising for firms to require a minimum level of assets under management to be able to provide the necessary revenue stream for a firm to take on the task of managing that type of account.

c. **Ranking Member Davis also stated that, "these cost restrictions would put us in a situation where these perverse incentives might force Members to engage in more market trading in order to meet blind-trust minimums and other requirements." What is your reaction to that statement?**

I believe that there could be incentives around the margins to conduct more trading or put more money in investments in order to meet a blind-trust requirement, but I do not believe that it is likely that blind-trust minimums themselves will encourage significantly more trading by Members.

d. **In general, Members of Congress may not use official or principal campaign committee funds for personal purposes. However, they may use both types of funds to pay for**

certain expenses that are incurred because of their responsibilities or obligations that exist only because of their position as a federal officeholder. In the event that modified standards for deterring financial conflicts of interest for certain covered officials require covered officials in certain situations to establish qualified blind trusts, should those officials be permitted to use official funds to defray the costs of establishing or maintaining such trusts?

I have no view as to whether such funds should be permitted to be used to defray blind trust costs.

4. **As shown at the hearing and in news reports, despite the existence of disclosure requirements, a number of covered officials have failed to comply with them. With respect to compliance and enforcement, you testified that, "It is worth examining whether the penalty framework is sufficiently deterrent and considering public reporting of delinquent disclosure." Similarly, another witness testified that, "the high-level principles to consider with an enforcement mechanism" include that "any penalties would be meaningful, that it would be easy and simple to apply, and that the public can have confidence that it is being applied evenly across the board," and "there has to be some transparency there." Another witness testified that, "the penalties aren't high enough to promote the compliance that I assume that Members want and that the public is demanding."**

   a. **What are reasonable additional penalties that Congress should consider that would promote compliance and provide a more meaningful penalty for violations?**

Please see my answer to question 1 above.

   b. **What specific suggestions do you have for reforming the existing penalty framework?**

Please see my answer to question 1 above.

   c. **Should penalties be set at the same level for all violations, or should penalties be connected in some way to the dollar value of reportable items that were not reported in compliance with the law?**

Please see my answer to question 1 above.

   d. **Should the length of tardiness of an outstanding public disclosure required by the law be a factor in the size of the penalty?**

Please see my answer to question 1 above.

   e. **Should the size of the penalty be determined in part by the number of prior violations by a covered official?**

Please see my answer to question 1 above.

5. **You observed in your testimony that "some of the questionable trading that happened during the COVID pandemic was in diversified funds" and that conflicts "are not nonexistent in diversified funds as well." Do you have any specific suggestions for additional measures to address or deter actual or possible conflicts of interest for covered officials with respect to financial interests in diversified funds?**

Diversified funds are not currently subject to reporting on periodic transaction reports, despite raising some of the same conflicts-of-interest concerns as other investments required to be reported.[3] Diversified fund transactions should not be exempt from periodic reporting.

6. **How should a reform proposal address holdings that covered officials may have in a privately held company that subsequently goes public?**

To the extent that a reform proposal requires the Member to take some action with respect to the public stock, the Member should be required to do so within a reasonable time frame. But this example illustrates the difficulties in drawing lines with respect to conflicts of interest. The conflict of interest existed for the Member while the company was private and continues while the company is public; it is not clear that these situations should be treated different from a conflicts-of-interest perspective. Enhanced transparency is a more consistent solution than requiring the Member to divest because the company became publicly traded.

7. **Is an "informal" blind trust where a third party manages the investment portfolio of the Member, and both the Member and the trust manager attest under penalty of perjury that no information on trades will be exchanged a viable alternative?**

This alternative may save on the legal fees required to establish a trust, but it is unlikely that there would be much cost-savings with respect to fees paid to the trustee and for management of the account. Moreover, there is a tradeoff for this "informal" arrangement: blind trusts themselves are not fool-proof, and such an informal arrangement is more likely to be subject to abuse that then more formal arrangement. Maintaining the "blindness" of either arrangement requires an exemption from public reporting of transactions, but given the higher potential for abuse, such a reporting exemption may not be desirable for an informal arrangement.

Questions from Committee Minority

- **How do you think Congress can internally strengthen its processes to help ensure Members (a) know about their requirements under the STOCK Act and (b) are able to comply with its requirements?**

Ensuring that Members know about their requirements under the STOCK Act seems to be a question of making sure that Members have access to information in a timely manner that

[3] U.S House of Representatives Committee on Ethics, Instruction Guide Financial Disclosure Statements and Periodic Transaction Reports Calendar Year 2021 at 42, available at https://ethics.house.gov/sites/ethics.house.gov/files/documents/FINAL%202021%20FD%20Instructions.pdf

alerts them to their responsibilities. The presentation of that information matters; such information may be lost in a flood of other information being conveyed to Members and the importance of compliance may not be being highlighted. These types of issues – financial reporting and conflicts of interest – are often the subject of annual training in the private sector (and in other government contexts), which recognizes the importance of the issue and ensures that information is repeatedly conveyed to recipients about the manner in which compliance is expected.

Streamlining compliance can also help Members to meet their obligations. Many private firms that have trading restrictions on their employees use automated software to help with compliance. While the needs of Congress may be different from an average private employer, it is worth considering whether any aspect of reporting can be automated to allow Members to "set it and forget it," so to speak.

- **Would a ban on trading have an impact on Americans, including those from younger generations and minorities, who may want to run for office in the future?**

A ban on trading may deter individuals from running for office to the extent that they are not interested in altering their investment behavior to hold elected office. This could happen for a number of reasons, including that it may be disruptive to long-term financial goals. Importantly, recent innovations in market access have made retail investing easier for many individuals, bringing a broader swath of the U.S. population into the markets.[4] Stock market participation has increased among Black and Hispanic populations and among younger individuals. This is a positive development, as a substantial portion of Americans—especially those who are less wealthy, younger, and more racially diverse—have traditionally been left out of the opportunities to grow wealth afforded by the stock market. Banning trading may limit the interest of some of these new investors in running for office—or cause them to choose to no longer invest—both of which would be undesirable outcomes.

- **Cryptocurrencies are becoming popular investments. What impact would a ban on crypto trading have on Congress' makeup?**

Investment in cryptocurrencies have been disproportionately popular with underrepresented populations. For example, a recent survey found that 25% of Black Americans own cryptocurrency, compared to only 15% of white investors.[5] For younger investors, 38% of Black investors under 40 own cryptocurrency, compared to 29% of white investors of the same age. Other survey results have found higher proportions of cryptocurrency investors among

---

[4] Jennifer J. Schulp, *GameStop and the Rise of Retail Trading*, Cato Journal (Fall 2021), available at https://www.cato.org/cato-journal/fall-2021/gamestop-rise-retail-trading.

[5] Charles Schwab, "Longstanding Disparity Between Black and White Investors Narrows, But New Risks Emerge," available at https://pressroom.aboutschwab.com/press-releases/press-release/2022/Longstanding-Disparity-Between-Black-and-White-Investors-Narrows-But-New-Risks-Emerge/default.aspx (reporting results of 2022 Ariel-Schwab Black Investor Survey).

Hispanics: 24% of crypto owners are Hispanic, while only 16% of the U.S. population identifies as Hispanic.[6] While data on these trends is still being collected and analyzed, in general, it appears that cryptocurrencies have been of interest in underrepresented communities.[7]

Unlike traditional equity investments, which some argue can be substituted with investments in diversified funds, there is no clear substitute for investment in cryptocurrencies. Moreover, because many cryptocurrencies are intended to be used as a method of payment, banning Members from holding crypto may have an even more dramatic effect on their ability to participate in the economy than restricting investment in publicly traded securities.

Any legislation addressing reporting or restrictions should be clear as to its effect on cryptocurrency investments. Crypto holdings are currently subject to reporting, as the House Ethics Committee considers cryptocurrencies to be "other forms of securities" to be reported on periodic transaction reports.[8] But when considering new legislation, its effect on cryptocurrency holdings should be explicitly contemplated, not left to later interpretation.

- **A big question regarding proposed reforms concerns Members' spouses and other family members. Unlike Members, these individuals didn't choose to run for Congress, yet they may be subject to the same conflict-of-interest concerns as Members. How should Congress strike an appropriate balance between autonomy and public transparency?**

Decisions about whether restrictions pose an undue burden on family members should be made by the Member and their family, but barring exceptional circumstances, spouses and dependent children should be subject to the same restrictions as Members. To establish a regime that exempts spouses and dependent family members from restrictions would create a loophole that could substantially undermine the regime's effectiveness. This question is less consequential when the question is of additional transparency rather than a ban in conduct, however, because spouses and dependents can retain more autonomy while providing additional transparency.

- **What is the impact of requiring individuals, such as Members of Congress, to divest a lifetime of assets when entering office?**

First and foremost, there could be significant tax consequences to divesting assets, particularly those that have been held long-term. In addition, a Member may be unable to rebuild their portfolio in the same manner when they leave Congress; for example, individuals who had

---

[6] Lorie Konish, "Why U.S. minority communities may turn to cryptocurrencies to pay their bills," CNBC (February 8, 2022), available at https://www.cnbc.com/2022/02/08/-research-shows-cryptocurrency-adoption-among-hispanics-is-high.html.

[7] *See* Leda Alvim and Lulit Tadesse, "Cryptocurrency attracting Black, Latino investors and fans," ABCNews (February 10, 2022), available at https://abcnews.go.com/Business/cryptocurrency-attracting-black-latino-investors-fans/story?id=82684748.

[8] U.S House of Representatives Committee on Ethics, Instruction Guide Financial Disclosure Statements and Periodic Transaction Reports Calendar Year 2021 at 19, available at https://ethics.house.gov/sites/ethics.house.gov/files/documents/FINAL%202021%20FD%20Instructions.pdf.

significant stock holdings as a consequence of prior employment may no longer be able to amass a similar position. Divestiture may force Members to have to sell stock that they have held for non-pecuniary reasons, such as a stake in a company important to their family or a gift from relatives. Requiring divestment may also dissuade individuals from seeking office who would prefer to not upend their investment portfolios.

- **How can we improve the public's confidence in Congress without disincentivizing people with financial experience from running for office?**

Improving the public's confidence in Congress is not a question that is limited to the trading activities of Members, and there is a danger that severely restricting Congressional trading will do little to increase public confidence so long as the public perceives that lawmakers continue to make decisions based on personal financial interests. But, as I stated in my written testimony, enhancing transparency permits voters to choose whether the conflicts faced by their elected representatives are problematic, even if those trades are perfectly legal. Providing voters with the information to make those choices limits unintended consequences of additional restrictions and puts the choices in the hands of the voters.

- **Some witnesses explained divestiture or qualified blind trusts as the only possible choices to address conflicts of interest and suggested a STOCK Act that encompasses that dichotomous framework. Is this the best way to consider the possibilities for reform?**

While divestiture or qualified blind trusts are options to consider in addressing conflicts of interest, they are not the only possibilities for addressing conflicts of interest and undue focus on these two options as curing conflicts overlooks the broader question of financial conflicts that will not be addressed by either of these options. As I stated in my written testimony, trading bans themselves have consequences, while not addressing the broader question of financial conflicts of interest that exist outside of traded securities. It is not clear that publicly traded securities pose a greater conflict of interest than other financial interests and thus should be subject to stronger restrictions. Enhancing transparency, on the other hand, can bring all conflicts of interest into the light, allowing voters to make decisions about which conflicts are problematic for their representation.

- **Should senior staff be covered by any complete trading ban or increased restrictions? If so, how should "senior staff" be defined?**

Senior staff are not subject to the same ballot box check that members are, and therefore it may be appropriate to consider the situation of senior staff separately from the question of Members and their dependents. Because senior staff can be privy to material, non-public information, or in positions with the ability to influence policy, restrictions may be appropriate as they are in other government or private sector jobs in which individuals are in a similar situation. Senior staff should be defined by job function, considering the likelihood of access to material, non-public information and the ability to exert influence over policy.

- **Should Congress implement a similar reporting regime modelled off Section 16(A) of the Securities and Exchange Act? Please explain.**

Section 16(a) of the Securities Exchange Act requires certain reporting of securities ownership by "insiders," i.e., directors and officers of the issuer of a security and those who are beneficial owners of more than 10 percent of certain equity securities.[9] Section 16 reporting includes what is known as Form 3, Form 4, and Form 5 reports. Form 3 must be filed with 10 days of any individual or entity becoming subject to the reporting requirement and includes the details of the insider's holdings. Form 4 must be filed within 2 business days of any transactions that change the insider's ownership interest in the securities—for example, any purchase or sale or any stock option grant or forfeiture. Form 5 is required in more specialized circumstances and is required to be filed no later than 45 days after the end of the public company's fiscal year.

The STOCK Act's requirement for periodic transaction reporting is already similar in that it requires reporting of transactions within a specified timeframe. The STOCK Act treats all Members (and other covered persons) as "insiders;" the annual financial disclosure can be thought of as Form 3, whereas the periodic transaction reports can be thought of as Form 4. What is notable is the stark differences between the STOCK Act and Form 4 with respect to the amount of time allowed between the transaction and the filing of the report. Please see my answer to question 2 above addressing my recommendations regarding the appropriate time frame for disclosure.

- **Would a pre-transaction disclosure requirement be a viable solution for Congress to address the calls for greater transparency?**

A pre-transaction disclosure requirement may be a useful tool in preventing unlawful insider trading. By pre-transaction disclosure, I mean a pre-clearance system whereby an individual who wants to make a transaction seeks clearance from an ethics officer prior to completing the transaction. This approach is not uncommon in the private sector; such approaches often require certain personnel who are identified as likely to have access to material, non-public information to submit a proposed transaction for approval prior to consummating the trade. The time frames for submitting a transaction for pre-clearance vary; companies sometime specify a minimum number of days prior to the transaction that the request must be made (for example, 2 days), but policies often provide no specific time frame for submission or for the response. Pre-clearance is often also employed in conjunction with trading blackout periods during which designated individuals are not permitted to trade at all, and with trading plans through which designated individuals may be permitted to trade pursuant to a pre-determined plan. A pre-clearance regime is not meant to handle quick turnaround trading decisions.

Pre-clearance can be logistically challenging and requires dedicated resources to be able to handle requests in a timely manner. In the private sector, pre-clearance usually applies to a

---

[9] *See* 15 U.S.C. § 78p(a) and 17 C.F.R. § 240.16a-2, *et seq.*

more limited number of personnel than would be at issue for any Congressional regime covering Members (or others). It also generally only applies to a more limited number of securities; for a public company, for example, it usually only applies to the company's own securities. For lawmakers, it is likely that the range of securities to be reviewed—and the potential types of material, non-public information to be considered—are wider, leading to additional challenges in implementing such a regime.

An additional challenge in the context of Congress, however, is ensuring that the process is insulated from political pressures and itself does not become a point of political conflict.

It is important to note that pre-transaction disclosure requirement does little to address broader conflict-of-interest concerns that arise where an individual's investments cause them to be financially interested in the effect of policy on a company. For this reason, pre-transaction disclosure is not a cure-all for calls for greater transparency that relate not just to insider trading concerns, but to broader conflicts of interest.

- **Are similar pre-transaction disclosure requirements employed in the private sector?**

Please see my answer above.

- **What time frames are used?**

Please see my answer above.

- **Would these time frames be appropriate for Congress?**

Please see my answer above.

- **What are the negative consequences of pre-transaction disclosure?**

Please see my answer above.

- **Do you see a minimum holding period for securities as a viable solution to address calls for greater transparency?**

A minimum holding period for securities may be a useful tool in preventing unlawful insider trading. Such holding periods are commonly employed in other contexts where there is a risk that an employee may be in possession of material, non-public information. For company insiders, the short swing profit prohibition of Section 16(b) of the Securities Exchange Act, imposes such a holding period as a practical matter.[10] Such holding periods can prevent a person from acting on material, non-public information and also can help to minimize the appearance of inappropriate insider trading. It is important to note, however, that a minimum holding period does little to address broader conflict-of-interest concerns that arise where an individual's investments cause them to be financially interested in the effect of policy on a company. For this reason, a minimum holding period is not a cure-all for calls for greater

[10] *See* 15 U.S.C. §78p(b).

transparency that relate not just to insider trading concerns, but to broader conflicts of interest.

SUBMISSIONS FOR THE RECORD

Congressional Research Service
Informing the legislative debate since 1914

Stock Trading in Congress: 117th Congress Proposals to Limit or Prohibit Certain Financial Transactions

February 17, 2022 (IN11860)

Jacob R. Straus, Specialist on the Congress (jstraus@crs.loc.gov, 7-6438)

On April 4, 2012, President Obama signed the STOCK Act (P.L. 112-105; Stop Trading on Congressional Knowledge Act of 2012). The STOCK Act, as amended, affirms that Members of Congress, congressional employees, and other federal officials are not exempt from "insider trading" laws and regulations and are required to file periodic transaction reports with their supervising ethics office within 30 days of a covered financial transaction. For the House of Representatives, the supervising ethics office is the House Ethics Committee, and for the Senate it is the Senate Select Committee on Ethics.

In the 117th Congress (2021-2022), there has been interest in further limiting or prohibiting Members of Congress and covered congressional employees from engaging in certain financial transactions. As of February 14, 2022, at least 12 bills or resolutions have been introduced to address this issue. These measures propose to amend the Ethics in Government Act (5 U.S.C. Appendix §§101-112), the STOCK Act, or House Rules to prohibit certain transactions, increase financial disclosure reporting requirements, and prescribe remedies and penalties for engaging in certain behaviors. **Figure 1** lists the 12 measures, the proposed affected party, the bill's or resolution's proposed actions, and the timeline for implementation, if enacted.

Figure 1. Proposals to Limit or Prohibit Certain Financial Transactions, 117th Congress

Bill or Resolution	Affected Congressional Party	Proposal	Timeline
H.Res. 873 No Option for Stock Trading and Ownership as a Check to Keep Congress Clean Resolution	Members of Congress, Delegates, and Resident Commissioner	Amends House Rule XXIII to prohibit ownership of common stock	Not specified
H.R. 459 HUMBLE Act	Members of Congress, Delegates, and Resident Commissioner	Amends House Rule XXIII to prohibit ownership of common stock	Effective immediately before noon on January 3, 2023
H.R. 336 TRUST in Congress Act	Members of Congress, spouses, and dependent children	Placement of covered investments in a qualified blind trust	Within 90 days of enactment for current Members or within 90 days of taking office for new Members
H.R. 1579 Ban Conflicted Trading Act S. 564 Ban Conflicted Trading Act	Members of Congress and congressional employees who file Financial Disclosure reports under the Ethics in Government Act	Prohibits purchase or sale of covered investments	Not specified
H.R. 6490 Banning Insider Trading in Congress Act S. 3504 Banning Insider Trading in Congress Act	Members of Congress and spouses	Amend the Ethics in Government Act to prohibit holding, purchase, or sale of covered financial instruments	Within 180 days of enactment for current Members or within 180 days of taking office for new Members
H.R. 6694 STOCK Act 2.0[a] S. 3612 STOCK Act 2.0	Members of Congress, senior congressional staff, spouses and dependents	Amend Ethics in Government Act to prohibit purchase or sale of covered financial instruments; and amend the STOCK Act to require public access to covered officials' financial disclosure and periodic transaction reports	Not specified
S. 3494 Ban Congressional Stock Trading Act	Members of Congress, spouses, and dependents	Amend the Ethics in Government Act to require the divestment or placement of covered investments in a qualified blind trust	Submit certification within 30 days of enactment for current Members or within 30 days of taking office for new Members Divest or place covered instruments in a qualified blind trust within 120 days of enactment or within 120 days of taking office for new Members
S. 3550 Ethics Reform Act	Members of Congress	Prohibit purchase or sale of individual securities	Not specified
S. 3631 Bipartisan Ban on Congressional Stock Ownership Act of 2022[b]	Members of Congress and spouses	Prohibit ownership of specified assets and requires divestment of assets except for widely held investment fund	Depending on type of asset, divest within 180 days or 5 years of enactment for current Members or within 180 days or 5 years of taking office for new Members

Source: CRS summary of proposed legislation.

Notes: To compile this list, CRS searched Congress.gov using subject headers "Government Ethics" + "Members of Congress" + "Securities." CRS supplemented this search by examining House dear colleague letters and Member press releases for similar legislation. It is possible that other measures that might address similar policy matters but use different wording were not captured by this search. Jennifer Manning, Senior Research Librarian, conducted the search on February 14, 2021.

a. Text of H.R. 6694 is not yet available on Congress.gov. For a summary of the bill, see a summary of

the measure on the sponsor's web page.
b. Text of S. 3631 is not yet available on Congress.gov. For bill text, see the link from the bill sponsor's web page.

Proposals to Limit or Prohibit Certain Financial Transactions

This Insight broadly describes the 12 measures proposed to regulate financial activities of Members of Congress and covered congressional staff. Generally, the proposals would prohibit covered individuals from the holding, purchase, sale, and/or active management of certain types of financial assets; amend the Ethics in Government Act and/or the STOCK Act; require certain assets to be placed in blind trusts; and/or amend House Rule XXIII to prohibit certain financial activities.

Prohibit Holding, Purchasing, and Selling Certain Assets

Eight proposals would generally prohibit covered officials from the holding, purchase, sale, and/or active management of certain types of assets. Aspects of these measures (H.R. 1579, H.R. 6490, H.R. 6694, S. 564, S. 3504, S. 3612, S. 3631, and S. 3550) would prohibit the purchase or sale of specified financial instruments, require additional disclosures and potential divestment, and/or increase penalties for noncompliance. Currently, Congress does not prohibit the ownership of specified financial assets, but some executive branch agencies do. For example, the Nuclear Regulatory Commission has supplemental Standards of Ethical Conduct that include a list of prohibited securities (5 C.F.R. §5801.102).

Amend Ethics in Government Act and/or the STOCK Act

Five proposals (H.R. 6490, H.R. 6694, S. 3494, S. 3504, and S. 3612) would amend the Ethics in Government Act and/or the STOCK Act. Broadly, they propose to amend the Ethics in Government Act to prohibit certain transactions and the holding of covered financial instruments. In some cases, the proposals would authorize the use of qualified blind trusts to avoid or prevent potential conflicts of interest. Further, two proposals (H.R. 6490 and S. 3504) would provide the supervising ethics office with the power to impose civil fines and require the Government Accountability Office (GAO) to audit compliance with the law.

Require the Use of Blind Trusts

A number of the proposals would allow or require a Member of Congress (and their spouses and/or dependent children) to place any covered assets in a qualified blind trust. Under the Ethics in Government Act, a qualified blind trust "confer[s] on an independent trustee and any other designated fiduciary the sole responsibility to administer the trust and to manage trust assets without participation by, or the knowledge of, any interested party or any representative of an interested party" (5 C.F.R. §2634.401(a)). Pursuant to the Ethics in Government Act (5 U.S.C. Appendix §102(f)(3)), a qualified blind trust must meet certain requirements, including that the trustee must be an independent actor, no restrictions can be placed on asset disposal, communication must be limited between the trustee and interested parties, and the supervisory ethics office must approve the trust.

Amend House Rule XXIII

Two proposals (H.R. 459 and H.Res. 873) would amend House Rule XXIII, the House Code of Conduct, to add a new section that would state

PROHIBITING MEMBERS OF HOUSE OF REPRESENTATIVES FROM OWNING INDIVIDUAL STOCKS.—A Member, Delegate, or Resident Commissioner may not own the common stock of any individual public corporation.

Amending House Rules to prohibit ownership of individual stocks might require the divestiture of certain assets by Members of the House. As an amendment to the Code of Conduct, jurisdiction over the implementation and enforcement of this proposed rule change would likely be under the jurisdiction of the House Ethics Committee. A similar proposal to amend Senate Rules has not been introduced.

The Honorable Nancy Pelosi

Speaker of the House of Representatives
235 Cannon House Office Building
Washington, D.C.
20515

The Honorable Zoe Lofgren
Chair
Committee on House Administration
1216 Longworth House Office Building
Washington, DC
20515

The Honorable Kevin McCarthy
Minority Leader of the House of Representatives
2421 Rayburn House Office Building
Washington, DC
20515

The Honorable Rodney Davis
Ranking Member
Committee on House Administration
1216 Longworth House Office Building
Washington, DC
20510

Madam Speaker, Minority Leader McCarthy, Chair Lofgren and Ranking Member Davis:

We, the undersigned organizations, are a broad and diverse group of good government organizations committed to ensuring that our institutions and elected officials act on behalf of the people they serve. It is with this purpose in mind that we write to urge you to support legislation prohibiting Members of Congress from owning or trading individual stocks, bonds or other similar financial investments.

Our country is at an inflection point: the reports of Members' suspicious stock trades at the beginning of the pandemic[1] and the routine and bipartisan failures to comply with the STOCK Act[2] have severely harmed public confidence in Congress.[3] This crisis of institutional legitimacy requires a swift and comprehensive response. We therefore urge you to pass legislation that addresses the full scope of the problem by eliminating a significant source of potential conflicts for Members.

We believe it is crucial that any legislation attempting to confront these problems include a blanket ban on trading or owning any individual stocks, bonds, commodities, futures, derivatives, options, or other similar financial assets, except widely held investment

---

[1] Jack Kelly, "Senators Accused of Insider Trading, Dumping Stocks After Coronavirus Briefing," *Forbes*, Mar. 20, 2020, *available at* https://www.forbes.com/sites/jackkelly/2020/03/20/senators-accused-of-insider-trading-dumping-stocks-after-coronavirus-briefings/?sh=6809d59f4a45.

[2] Dave Levinthal, "54 members of Congress have violated a law designed to stop insider trading and prevent conflicts-of-interest," *Business Insider*, Jan. 11, 2022, *available at* https://www.businessinsider.com/congress-stock-act-violations-senate-house-trading-2021-9.

[3] Kedric Payne, Delaney Marsco, and Sophia Gonsalves-Brown, "Congressional Stock Trading During Pandemic Diminishes Public Trust," *Campaign Legal Center*, Apr. 28, 2020, *available at* https://campaignlegal.org/update/congressional-stock-trading-during-pandemic-diminishes-public-trust.

funds. We believe that placing assets into a qualified blind trust would only solve this problem if the beneficiary does not know what assets the trust holds. This means that trustees must be directed to sell all the Member's individual assets, and Members must not be permitted to retain any individual assets held prior to joining Congress.

The prohibition must also extend to Members' spouses or dependent children: Members must not be permitted to simply transfer their individual assets to a close family member. A carve-out for spouses and dependent children would undermine much of the purpose of the legislation and allow the conflicts of interest presented to remain. A spouse or dependent child who appears to profit from a Member's actions or knowledge of the market is just as damaging to the public's perception of our government as a Member profiting themselves.

Finally, Congress must ensure that the bill's enforcement mechanism is both clear enough that Members understand precisely what will happen should they violate the act, and significant enough to serve as a functional deterrent. Specifically, it is crucial that Members understand that they will be subject to punishment or civil penalties if they violate the act: decades of academic research have proved that the certainty of sanction is the best deterrent.[4] With that in mind, the legislation must not create an exclusive intent standard that would make enforcement of the legislation unworkable or unlikely. For example, a standard requiring proof that a member "knowingly" violated the act would make a very high bar for any enforcement and accountability for unethical conduct. Such a standard would defeat the purpose of the legislation, as it would likely result in Members believing that they can escape discipline and even potentially retain the benefits of trades made in violation of the law.

The American people widely support these policies across partisan lines[5] and are calling on Congress to act.[6] They have given you a mandate to pass bold, comprehensive legislation.[7] By adopting the policies that we have set out above, you can help to end this problem that is eroding public trust in our government and undermining Congress's legitimacy.

---

[4] *See, e.g.*, Valerie Wright, "Deterrence in Criminal Justice: Evaluating Certainty vs. Severity of Punishment," The Sentencing Project, Nov. 2010, *available at* https://www.sentencingproject.org/wp-content/uploads/2016/01/Deterrence-in-Criminal-Justice.pdf.

[5] Jon Green and Mark White, "The Public Thinks Members of Congress Shouldn't Be Able to Own Individual Stocks," *Data for Progress*, Mar. 19, 2020, *available at* https://www.dataforprogress.org/blog/2020/3/19/the-public-thinks-members-of-congress-shouldnt-be-able-to-own-individual-stocks .

[6] Claire Williams, "Most Voters of All Parties Support Congressional Stock Trading Restrictions," *Morning Consult*, Jan. 19, 2022, *available at* https://morningconsult.com/2022/01/19/ban-stock-trading-congress-poll/.

[7] Olafimihan Oshin, "Two-thirds of Americans support banning lawmakers from trading stocks: poll," *The Hill*, Jan. 18, 2022, *available at* https://thehill.com/homenews/house/590216-two-thirds-of-americans-support-banning-lawmakers-from-trading-stocks-new-poll.

Our democracy is facing the largest crisis of public trust in a generation. Thankfully, you now have in your hands the tools to rebuild trust in our government and a mandate to use them. We look forward to working with you to pass this critical legislation and send President Biden the first comprehensive Congressional ethics legislation in almost a decade. Thank you for your attention to this matter.

Sincerely,

Campaign Legal Center
Center for Biological Diversity
Citizens for Responsibility and Ethics in Washington (CREW)
CommonDefense.us
DemCast USA
Democracy 21
The Digital Democracy Project
Fix Democracy First
Indivisible
Mainers for Accountable Leadership Action
Michiganders For Fair & Transparent Elections
MoveOn
Peace Action
Progressive Change Campaign Committee
Public Citizen
Revolving Door Project
SMART Legislation
Stand Up America
Transparency International U.S. Office

Gonzaga University School of Law

Legal Studies Research Paper No. 2016-14

THE SHORTSIGHTEDNESS OF BLIND TRUSTS

MEGAN J. BALLARD

The Shortsightedness of Blind Trusts

Megan J. Ballard[*]

I. INTRODUCTION

In June 2005, Senate Majority Leader Bill Frist directed the trustees of his family's thirteen trusts to sell all stock in HCA—the hospital company established by Frist's father and brother, the nation's largest hospital chain.[1] This would have been an unremarkable event, except for the fact that all thirteen trusts were established as blind trusts for the benefit of Bill Frist and his immediate family members.[2] This blindness theoretically meant the trustees kept the former Senator and his family in the dark about the identity and management of the assets held in trust.

Policymakers enter government service owning assets and having private investment interests just like other people. Policymakers' private economic concerns may, however, present conflicts of interest with official decision-making.[3] The Federal Ethics in Government Act

* Associate Professor, Gonzaga University School of Law. I am grateful for very helpful comments from Linda Rusch, Mary Pat Treuthart, James Celto Vaché, and Vickie Williams. My thanks also to Bo Howell, Merri Hartse and especially to Laura Reed for outstanding research assistance.

1. Len Costa, *A Wink and a Nod*, LEGAL AFF., Jan.–Feb. 2006, at 18, 18.

2. *Id.* In addition, the timing of the sale was suspicious: the sale preceded a poor earnings report that caused the stock price to plummet by about nine percent in one day. *Id.* The Securities and Exchange Commission and the U.S. Department of Justice began an inquiry into the sale in September 2005 to investigate whether Frist improperly acted on any inside information. Jeffrey H. Birnbaum & R. Jeffrey Smith, *SEC, Justice Investigate Frist's Sale of Stock*, WASH. POST, Sept. 24, 2005, at A1. Frist denied any wrongdoing, asserting that he ordered the stock divestiture to avoid conflicts of interest as he contemplated a 2008 bid for the presidency. Carrie Johnson & Jeffrey H. Birnbaum, *SEC Issues Subpoena to Frist, Sources Say*, WASH. POST, Oct. 13, 2005, at A1.

3. There is no set definition of a conflict of interest. A broad interpretation is that a conflict of interest arises if 1) a person is in a relationship with another individual or a group that requires the person to exercise judgment on behalf of the individual or group, and 2) the person has an interest that tends "to interfere with the proper exercise of judgment in that relationship." Michael Davis, *Introduction* to CONFLICT OF INTEREST IN THE PROFESSIONS 3, 8 (Michael Davis & Andrew Stark eds., 2001). The Ethics Manual for the U.S. House of Representatives presents a more narrow definition, considering that the term "'denotes a situation in which an official's conduct of his office conflicts with his private economic affairs.'" COMM. ON STANDARDS OF OFFICIAL CONDUCT, U.S. HOUSE OF REPRESENTATIVES, ETHICS MANUAL FOR MEMBERS, OFFICERS, AND EMPLOYEES OF THE U.S. HOUSE OF REPRESENTATIVES 87 (1992) [hereinafter HOUSE ETHICS MANUAL] (quoting ROBERT S. GETZ, CONGRESSIONAL ETHICS 3 (1966)). The Ethics Manual continues: "The ultimate concern, 'then, is risk of impairment of impartial judgment, a risk which arises whenever there is temptation

requires certain national policymakers and employees to publicly disclose their financial interests on an annual basis.[4] Disclosing private economic matters allows the public to monitor potential financial conflicts of interest. Such disclosure need not detail specific assets when a policymaker opts to transfer his financial interests into a blind trust. The blind trust, then, operates as an exception to complete financial disclosure while, at the same time, attempting to shield a policymaker from conflicts of interest. Nonetheless, this shield functions properly only if the policymaker is actually blind to the identity and management of the assets once he has transferred them into the trust.[5]

Frist was not blind to the assets in his blind trusts. He received numerous updates from his trustees regarding the identity of certain trust assets, including the trust's hospital stock holdings.[6] One trustee reported to the Senate that he told Frist in 2002 that HCA stock had been transferred into one of the trusts.[7] Apparently, the trustee informed Frist on several occasions that HCA stock worth hundreds of thousands of dollars was placed into Frist's blind trusts.[8]

Despite this notification, Frist publicly claimed to have no knowledge of the assets in his family's blind trusts. Frist asserted in a January 2003 television interview "that he did not know how much HCA stock he owned, if any," because he had transferred his assets into a blind trust.[9] He hid behind the blind trust shield to assuage the public's

---

to serve personal interests.'" *Id.* (quoting JAMES C. KIRBY, JR., CONGRESS AND THE PUBLIC TRUST 39 (1970)). Interestingly, the term "conflict of interest" appears to be a relatively recent invention of the latter half of the 20th century. Black's Law Dictionary did not include a definition of "conflict of interest" until 1979. The Index of Legal Periodicals did not include a "conflict of interest" subject heading until 1967. Davis, *supra*, at 17. Nonetheless, the concept seems to have much earlier origins. For example, the U.S. Constitution forbids federal officials from "accepting gifts, employment, or titles from foreign governments." Kathleen Clark, *Regulating the Conflict of Interest of Government Officials*, *in* CONFLICT OF INTEREST IN THE PROFESSIONS, *supra*, at 49, 49 (citing U.S. CONST. art. I, § 9, cl. 8).

4. 5 U.S.C. app. § 102(a) (2000).

5. Investments a policymaker transfers into a new blind trust will not suddenly become unidentifiable to that public official. Federal law attempts to address this problem. *See infra* notes 42–43 and accompanying text.

6. Costa, *supra* note 1, at 19 ("In a series of letters written to Frist between 2001 and 2005 and filed with the Senate Ethics Committee, the trustees informed him when HCA stock and other shares were purchased or sold on behalf of the trusts.").

7. Birnbaum & Smith, *supra* note 2. The majority of the Frist family's blind trust assets were managed by M. Kirk Scobey, Jr., president of Equitable Trust Company of Tennessee. David D. Kirkpatrick, *Frist Sale of Hospital Stock Spurs Inquiries into Trusts*, N.Y. TIMES, Sept. 24, 2005, at A8. Northern Trust, a Chicago-based company, managed other trusts, all of which sold HCA stock. *Id.*

8. Birnbaum & Smith, *supra* note 2; *see also supra* note 6 (referring to letters that Frist received from his trustees).

9. *Id.*

concerns about potential conflicts of interest.[10] Similarly, Frist's financial disclosure reports for 2004 and 2005 assert that he did not know of the underlying assets in most of his blind trusts.[11]

The former Senator's hospital investments raise concern because he was directly involved in crafting legislation that affected the health care industry.[12] Was his policymaking guided by the best interests of his constituents and the nation, or by his interest in furthering, or at least not hindering, the profitability of his family's hospital corporation?[13]

More recently, presidential candidate and Senator Barack Obama attempted to establish a blind trust that turned out not to be blind to him, causing even more public unease over the effectiveness of blind trusts. In 2005, Senator Obama acquired stock in a biotechnology concern developing an avian flu treatment, and then introduced a bill urging more research on avian flu drugs.[14] Obama claimed that his broker purchased the stock pursuant to a blind trust agreement that had not yet been finalized, and that he did not learn of this investment until months later.[15]

As a conflict avoidance measure, the blind trust seeks to strike a balance between two competing public interests. We want to encourage qualified individuals to participate in government service. At the same time, however, we need to ensure that government decisions are not

10. Larry Margasak, *Documents Show Frist Keeping an Eye on His Blind Trust; SEC Investigating Sale of Hospital Stock*, COLUMBIAN, Sept. 25, 2005, at A6 (quoting Frist as having asserted: "Well, I think really for our viewers it should be understood that I put this into a blind trust. So far as I know, I own no HCA stock"). Two weeks before this interview, a trustee for the majority of the Frist family's blind trusts informed Frist that one of his blind trusts had acquired HCA stock valued between $15,000 and $50,000. Jeffrey H. Birnbaum, *Letters Show Frist Notified of Stocks in 'Blind' Trusts*, WASH. POST, Oct. 24, 2005, at A1.

11. In both years, Frist did list assets in one blind trust. The assets appear to be mostly real estate holdings; none is hospital corporation stock. William H. Frist, United States Senate Financial Disclosure Report for Annual and Termination Reports (May 15, 2006), *available at* http://www.opensecrets.org/pfds/pfd2005/N00003147_2005.pdf; William H. Frist, United States Senate Financial Disclosure Report for Annual and Termination Reports (May 16, 2005), *available at* http://www.opensecrets.org/pfd2004/NOOOO3147_2004.pdf.

12. Frist served in the U.S. Senate from January 1995 to January 2007. He singled out health care as a special concern during these years of service. Sheryl Gay Stolberg, *For Frist, a Political Fortune May Be Inextricably Linked to a Financial One*, N.Y. TIMES, Oct. 25, 2005, at A19. In 1995, Frist supported a bill that increased Medicare reimbursements to for-profit hospitals, such as those owned by HCA. *Id.* Frist participated in 1997 on a bipartisan commission to recommend changes to Medicare. *Id.* Frist also played a key role in amending Medicare in 2003 by adding a voluntary prescription drug benefit. *Id.*

13. Frist maintains he did nothing wrong regarding his blind trusts. He stated that he consulted with outside counsel and Senate Ethics Committee staff before selling HCA shares. Costa, *supra* note 1, at 19. Indeed, the Senate Select Committee on Ethics absolved Senator Frist of any wrongdoing in relation to his blind trusts. Stolberg, *supra* note 12, at A19.

14. Mike McIntire & Christopher Drew, *Obama, in Brief Investing Foray in '05, Took Same Path as Donors*, N.Y. TIMES, Mar. 7, 2007, at A1.

15. *Id.*

tainted by a policymaker's own financial interests.[16] Valuing the latter concern can impair the former and vice versa. In other words, constructing absolute protections against financial conflicts of interest might mean complete disclosure of financial matters and divestiture of troublesome investments. Such limited options might discourage individuals from considering government employment. Blind trusts theoretically allow both interests to coexist peacefully. A critical evaluation of federal law regulating blind trusts, however, reveals that the use of blind trusts may err on the side of encouraging service to the public detriment of allowing policymakers' actions to be influenced by private financial concerns.

Exploration of the value of the blind trust vehicle in the public sphere merits immediate attention for a number of reasons. Disconcerting news reports regarding Senator Frist's and Senator Obama's blind trust investments undermine public confidence that these devices can prevent or deter financial conflicts of interest.[17] At the same time, blind trusts are increasingly being touted as a solution to conflicts

16. These competing public policy interests are not novel. They played a part in congressional debates over enacting conflict of interest legislation in 1962. The Senate report on the proposed legislation commented on then-existing ethics statutes that created "wholly unnecessary obstacles to recruiting qualified people for government service." S. REP. NO. 87-2213 (1962), *reprinted in* 1962 U.S.C.C.A.N. 3852, 3854. President-elect Carter apparently had these same public policy interests in mind. The ethics guidelines released by Carter's transition group before his inauguration recognized that "[t]o decree that no person can have any financial interests other than a salary from the Government would seriously limit the ability to recruit the most qualified persons." *Texts of Carter Statement on Conflicts of Interest and Ethics; Appointees' Guidelines*, N.Y. TIMES, Jan. 5, 1977, at A17.

17. Recent convictions of White House and congressional policymakers found to have used their power for personal gain further underscore the need to examine how to deter government officials from making decisions influenced by private financial interests. Representative Bob Ney agreed in September 2006 to plead guilty to charges related to gifts he received from lobbyist Jack Abramoff, after having denied that official actions previously taken on behalf of Abramoff were related to the gifts. Philip Shenon, *Ohio Congressman Is Said to Agree to Plead Guilty*, N.Y. TIMES, Sept. 15, 2006, at A14. A former White House budget official was convicted in June 2006 after lying to federal investigators about providing private assistance to Abramoff, his former lobbying partner. Philip Shenon, *Man Linked to Abramoff Is Sentenced to 18 Months*, N.Y. TIMES, Oct. 28, 2006, at A9. "A former top aide to Representative Tom DeLay" pleaded guilty in March 2006 to corruption charges stemming from his receipt of thousands of dollars in illegal gifts in exchange for influencing legislation. Philip Shenon, *Ex-DeLay Aide Pleads Guilty in Lobby Case*, N.Y. TIMES, Apr. 1, 2006, at A1. Representative Randy Cunningham pleaded guilty in November 2005, after acknowledging acceptance of "at least $2.4 million in bribes," including hundreds of thousands of dollars in cash and other gifts from two military contractors while helping them win Pentagon contracts. John M. Broder & Carl Hulse, *Republicans Denounce Ex-Lawmaker*, N.Y. TIMES, Nov. 30, 2005, at A29. Congress responded to concerns prompted by these convictions by enacting the Honest Leadership and Open Government Act of 2007, Pub. L. 110-81, 121 Stat. 735 *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:pub 1081.110.pdf (strengthening the disclosure requirements and enforcement of lobbying laws, among other purposes).

of interest in the private sector, "particularly given the nature of executive compensation, the business insider's need to diversify and manage portfolio risk, the critical focus on corporate governance, and increased regulation."[18] While private use of these devices is on the rise, there is no universal definition of a "blind trust" or established rules for its operation.[19] Similarly, some state legislatures have authorized the use of blind trusts by certain state officials as an alternative to financial disclosure.[20] These state blind trust rules are no more uniform than those for private blind trusts. Public unease over the effectiveness of federal blind trust rules, as well as the possibility that federal law may set a benchmark for private or state blind trusts, indicates a need to closely scrutinize the current federal statutory scheme.

This Article examines the blind trust, as presently authorized by federal law, and argues that the device does not provide sufficient protection against financial conflicts of interest for policymakers.[21] The

---

18. Edmond M. Ianni, *Blind Trusts Offer Clients Customized Wealth Planning*, 30 EST. PLAN. 319, 322 (2003). The Securities and Exchange Commission rule 10b5-1 (17 C.F.R. § 240.10b5-1 (2006)), which took effect in October 2000, allows executives to delegate the purchase or sale of shares in their own companies' stocks to a third party. Eric Schellhorn, *A New Take on the 'Blind Trust,'* CHRISTIAN SCI. MONITOR, Jan. 14, 2002, at 20. Yahoo!, Inc. co-founder Jerry Yang established a blind trust under Rule 10b5-1 to trade Yahoo! stock. Yahoo! Inc. Current Report (Form 8-K) (June 10, 2002); Edmond M. Ianni, *Remove Temptation*, TR. & EST., June 2003, at 42, 45 [hereinafter *Temptation*].

19. *Temptation*, *supra* note 18, at 43.

20. *See, e.g.*, Act of July 9, 2007, ch. 47, sec. 57, § 39.50.040, 2007 Alaska Adv. Legis. Serv. 47 (LexisNexis); CAL. CODE REGS. tit. 2, § 18235(a) (2000); CONN. GEN. STAT. ANN. §§ 1-79(a), 1-83 (West Supp. 2007); MD. CODE REGS. 19A.06.01.01–03 (2007). This Article does not thoroughly explore and analyze state blind trust rules, but it does draw on some features of different state rules to suggest amendments to federal legislation.

21. This Article does not address whether judges should be allowed to employ blind trusts as a means of avoiding financial disclosure. While federal judges and magistrates must adhere to the Ethics in Government Act's financial disclosure mandates, they are prohibited from using blind trusts as an exception to disclosure. Pub. L. No. 93-512, § 455, 88 Stat. 1609, 1609 (1974) (codified as amended at 28 U.S.C. § 455) (requiring federal judges and magistrates to disqualify themselves in any proceedings in which their impartiality might reasonably be questioned). The amendment makes the statutory disqualification rules conform to the Code of Judicial Conduct rules regarding disqualification, which the Judicial Conference adopted in 1973. H.R. REP. NO. 93-1453 (1974), *reprinted in* 1974 U.S.C.C.A.N. 6351, 6352–53. The House Judiciary Committee Report on this legislation unambiguously states that a judge's duty to inform himself about his financial interests "precludes use of a so-called blind trust." *Id.* at 6356. Ironically, the Committee reasoned that a blind trust is not blind because the judge would still have to report profit, loss or earnings from the trust property on his income tax report. *Id.* Members of Congress and executive branch officials also must report this data on their tax returns, yet a blind trust is still considered to be a sufficient conflict of interest shield for them. *See infra* note 41 and accompanying text (statute authorizes a trustee to communicate information about a blind trust that will allow the policymaker to complete an income tax return). Congress specifically requires judges to be informed of their financial interests. A federal judge or magistrate must "inform himself about his personal and fiduciary financial interests." 28 U.S.C. § 455(c) (2000). Whether judges should be allowed to rely on blind trusts is beyond the scope of this Article.

weaknesses of blind trusts result in two related injuries. First, because the rules for these trusts do not include sufficient incentives to maintain blindness, they may fail to prevent conflicts of interest. Policymakers knowledgeable about the financial assets they hold in a blind trust are in a position to make decisions influenced by a personal stake in the matter. Second, blind trusts can mislead the public into believing that policymakers are avoiding conflicts, when they may not be doing so.[22] Blind trusts that are not truly blind to a policymaker tend to disguise actual or apparent conflicts of interest from public oversight. In this sense, blind trusts undermine the transparency essential to democratic governance.

To explore the deficiencies of blind trusts, Part II of this Article discusses the current use and legislative parameters of the "qualified blind trust" established under the 1978 Ethics in Government Act. This part also briefly reviews events that led to the codification of blind trust rules, underscoring that some of the problems initially prompting the legislation continue to exist today.

Part III describes how a private trust is used as an asset-management device, and analyzes the ways in which this traditional trust differs from a blind trust. Under a traditional trust, an outside trustee can effectively manage assets for a beneficiary because the beneficiary's self-interest motivates him to monitor the trustee's performance.[23] A trustee's fiduciary obligation facilitates this oversight because a trustee must keep the beneficiary informed about the trust assets. Under a qualified blind trust, however, the beneficiary must be kept in the dark about his assets, contrary to his immediate self-interest. This fundamental difference gives rise to many of the flaws of blind trusts. Part III also discusses legislative attempts to compensate for a beneficiary's inability to act on his self-interest and oversee the trustee's performance. Finally, Part III maintains that these statutory efforts fail largely because there is no one else monitoring the trustee. This failure means that beneficiaries have a

---

22. Senator Frist is not the only public official to claim a blind trust absolves him completely of any potential conflict of interest, despite knowledge of the initial assets. Then Representative Thomas J. Bliley, Jr., criticized for potential conflicts between his role as chairman of the House Commerce Committee and his investment portfolio, responded by vowing to create a blind trust. He claimed that "'[o]nce the trust is created, I will not know what I own, so that no one can claim that my decisions are based on my own self-interest.'" David S. Cloud, *Bliley Investments Go to Blind Trust*, 53 CONG. Q. 1613 (1995).

23. To the extent the trust is established for the benefit of a minor child or incompetent adult, a parent, guardian, or conservator usually will be responsible for protecting the beneficiary's interests. UNIF. TRUST CODE § 303 (2000) (amended 2005).

strong incentive to ignore the statutory restrictions on communicating with trustees.

Part IV presents proposals to address the flaws of blind trusts. It begins by recommending that the device should not be used as an exception to financial disclosure. Because blind trusts are ineffective as a means of avoiding conflicts of interest, a choice must be made between encouraging a broader pool of possible public servants and protecting the integrity of government decisions. Public policy should place a higher value on preserving the decision-making process. Government decision-makers should fully disclose their financial affairs. Where a financial conflict of interest arises, a public official should refrain from decision-making or divest himself of the asset. While this Part addresses the advantages of complete financial disclosure, it also recognizes problems inherent in this approach. Given that Congress has already rejected disclosure coupled with abstention as a solution, Part IV concludes with proposals for amending the statute governing qualified blind trusts in ways that will, among other things, help to ensure a trustee is adequately monitored so that a public official has less incentive to remove the blindfold by seeking prohibited information regarding trust assets.

II. CURRENT BLIND TRUST RULES

A. *Qualified Blind Trusts Under the Ethics in Government Act*

The Ethics in Government Act of 1978 formally established the "qualified blind trust" as an optional mechanism for circumventing full disclosure of financial interests while at the same time avoiding conflicts with official duties.[24] Until this enactment, there was no authoritative consensus as to what elements constituted a proper blind trust.[25] To understand the role of blind trusts, it is useful first to review the financial disclosure mandate of the Ethics in Government Act and earlier conflict of interest legislation governing the executive branch.

The Ethics in Government Act, as amended, requires certain employees and officials from all three branches of government to submit financial disclosure statements accessible to the public.[26] The purpose of

24. Ethics in Government Act of 1978, Pub. L. No. 95-521, 92 Stat. 1824.

25. Office of Government Ethics, Advisory Opinion 86 x 12 (Sept. 8, 1986), *available at* http://www.usoge.gov/pages/advisory_opinions/advop_files/1986/86x12.pdf.

26. 5 U.S.C. app. §§ 101–102 (2000). Before this enactment, public officials were required to disclose their financial interests, but these disclosures were not made public. *Public Officials Integrity Act of 1977, Blind Trusts and Other Conflict of Interest Matters: Hearings on S. 555 Before*

disclosing financial interests is to facilitate public monitoring of, and to deter, conflicts of interest.[27] Persons who must report include the President, the Vice President, high-level executive branch employees, administrative law judges, members of Congress, high-level congressional officers and employees, federal judges, and federal judicial employees authorized to perform adjudicatory functions (collectively referred to as "reporting individuals").[28] At least annually, each reporting individual must disclose the source, type, and amount of income he received,[29] as well as the identity and general value of the property he owns.[30] For example, if a reporting individual owns Acme stock worth $95,000, and earns dividends of $4000 during a calendar year, that person's annual financial disclosure report must list the name of the corporation issuing the stock, mark the value of the asset as falling in the $50,000 to $100,000 category, and list dividends in the category of "greater than $2500 but not more than $5000."[31] This disclosure obligation extends to the financial interests of the reporting individual's spouse and dependent children.[32]

Financial disclosure obligations may require these same steps even if the Acme stock is held in a traditional trust that benefits the reporting individual. In general, the identity and value category of the underlying assets held by a traditional trust must be disclosed if the reporting individual has a beneficial interest in the trust.[33] However, the underlying assets of a trust need not be disclosed if they are held in a qualified blind trust.[34]

---

the S. Comm. on Governmental Affairs, 95th Cong. 7 (1977) (statement of President Carter to Congress proposing the Ethics in Government Act of 1977).

27. HOUSE ETHICS MANUAL, *supra* note 3, at 157.

28. 5 U.S.C. app. § 101(f)(1)–(12) (2000). Officers and employees are required to report if they are in a position classified above GS-15 of the General Schedule, or earn pay equal to or greater than 120 percent of the minimum rate of basic pay payable for GS-15 of the General Schedule. *Id.* §§ 101(f)(3), 101(f)(6), 109(13).

29. *Id.* § 102(a)(1). Reporting individuals must disclose the actual amount of earned income, other than income earned from current employment with the U.S. government. *Id.* § 102(a)(1)(A). In addition, reporting individuals must indicate a general value category of income from publicly traded and non-publicly traded assets and unearned income sources. *See id.* § 102(a)(1)(B) (requiring the reporting of "dividends, rents, interest, and capital gains").

30. *Id.* § 102(a)(3).

31. *Id.* § 102(a)(1)(B)(iii). Dividends and income must be reported when they accrue, even if dividends are automatically reinvested. U.S. OFFICE OF GOV'T ETHICS, PUBLIC FINANCIAL DISCLOSURE: A REVIEWER'S REFERENCE 8-10 (2d ed. 2004) [hereinafter REVIEWER'S REFERENCE].

32. 5 U.S.C. app. § 102(e)(1). Subsequent discussion of rules governing reporting individuals also applies to spouses and dependent children without specifically referencing these family members.

33. REVIEWER'S REFERENCE, *supra* note 31, at 7-27.

34. 5 U.S.C. app. § 102(f)(2)(A). The Ethics in Government Act also provides exceptions to financial disclosure for limited types of trusts and for assets held in a "widely held investment fund."

A reporting individual who chooses to transfer assets into a qualified blind trust need not separate out on a financial disclosure report the exact assets held by the trust. For example, if the qualified blind trust holds Acme stock, the financial disclosure report would not name the Acme Corporation, but would include only the name of the trust. The reporting individual must also identify the trust as a qualified blind trust, report the value range of the individual's interest in the trust, and report the value range of income that the individual received from the trust. While reporting individuals are not required to establish blind trusts, they are an attractive alternative to disclosure for some public policymakers.

In addition to the specific financial disclosure requirements that the Ethics in Government Act imposes on certain officials from all three branches of government, separate legislation imposes liability on executive branch employees related to financial conflicts of interest. Any employee of the executive branch who participates in a decision, on a matter in which, "to his knowledge," he has a financial interest, is subject to civil and criminal liability.[35] Blind trusts also provide an exception to this general conflict of interest legislation. Holdings in a blind trust are not considered to be a "financial interest" for purposes of this conflict of interest statute.[36]

So far, this section has described how a qualified blind trust limits both financial disclosure obligations, and the applicability of penalties for an executive branch employee's conflict of interest. The remainder addresses restrictions imposed on communication between a trustee and a beneficiary, as well as limitations on who may serve as a trustee. These are the provisions that attempt to render a trust blind to the beneficiary.

The qualified blind trust rules limit communication between a trustee and an "interested party"—a reporting individual or the individual's

A reporting individual need not report the underlying assets of a trust when the reporting individual did not establish the trust, and neither the reporting individual nor his spouse or dependent children know what is contained in the trust. *Id.* § 102(f)(2)(B). Examples of widely held investment funds include "a mutual fund, a regulated investment company, and a pension or deferred compensation plan." *Id.* § 102(f)(8). To qualify for this investment fund exception, such funds must not be controlled by the reporting individual and must be publicly traded or widely diversified. *Id.* § 102(f)(8)(A), (B).

35. 18 U.S.C. § 208(a) (2000). The current statutory prohibition stemmed from alleged civil war era abuses likely involving government officials making decisions about matters in which they had a personal interest. BAYLESS MANNING, FEDERAL CONFLICT OF INTEREST LAW 110 (1964). Section 208, enacted in 1963, is a "direct lineal descendant" of the former § 434. *Id.* at 109. Section 434, enacted in 1958, was in turn based substantially on an 1863 amendment to an 1862 act. *Id.* at app. A, 274–76, 280–81.

36. 5 C.F.R. § 2634.401(a)(1)(ii) (2007).

spouse and dependent children.[37] In managing the assets, a trustee "shall not consult or notify any interested party."[38] With few exceptions, the trustee may not provide any specific information on the trust assets or sources of income, and communication between any interested party and the trustee is limited.[39]

There are three general types of authorized communication. First, a trustee and interested party may communicate in writing about the "general financial interest and needs of the interested party," a direction to the trustee to sell all of an asset initially placed in the trust if it poses an actual or apparent conflict of interest, or notification of a law or regulation that prohibits the interested party from holding an asset.[40] Second, a trustee may provide quarterly reports to an interested party regarding the total value of that party's interest in the trust, the net income or loss of the trust, any information necessary to enable an interested party to complete an individual tax return, and information that will allow a reporting individual to complete a financial disclosure report.[41] Third, a trustee must notify the interested party when an asset initially placed in the trust is transferred out of the trust.[42] When a public official first establishes a qualified blind trust, it cannot actually be "blind." By virtue of the newness of the trust, the official knows what assets he transferred into it until a trustee notifies him that the trust no longer holds the asset. There is a limited statutory exception that allows a well-diversified portfolio placed in trust to be truly blind from its inception.[43] Absent this exception, or notice from a trustee, a public official must treat those assets as reportable financial interests.[44] Nonetheless, there appears to be no requirement that the reporting

37. 5 U.S.C. app. § 102(f)(3)(E) (2000) (defining "interested party" for purposes of qualified blind trusts as "a reporting individual, his spouse, and any other minor or dependent child").

38. *Id.* § 102(f)(3)(C)(i).

39. *Id.* § 102(f)(3)(C)(v).

40. *Id.* § 102(f)(3)(C)(vi).

41. *Id.* § 102(f)(3)(C)(v).

42. *Id.* § 102(f)(3)(C)(iii).

43. A blind trust that is established with only "a well-diversified portfolio of readily marketable securities" that do not consist of "securities of entities having substantial activities in the area of the reporting individual's primary area of responsibility" is considered completely blind from its inception. *Id.* § 102(f)(4)(B)(i). Accordingly, the reporting individual need not consider the initial assets to be financial interests for the purposes of § 102(f)(4)(A). *Id.* § 102(f)(4)(B)(i). Regulations governing executive branch blind trusts refer to blind trusts established with diversified assets as Qualified Diversified Trusts. 5 C.F.R. §§ 2634.401(a)(1)(iii), 2634.404 (2007).

44. 5 U.S.C. app. § 102(f)(4)(A) (2000). Treating the initial assets as a financial interest of the official means that the official will be subject to conflict of interest statutes, including 18 U.S.C. § 208 (prohibiting executive branch and independent agency officers and employees from taking government action while having a conflicting financial interest).

individual separately list these initial assets on a public financial disclosure form each year until the time the trustee provides notice that the asset has been transferred from the trust.[45]

To facilitate blindness, a trustee must be independent from any interested party. To be independent, a trustee cannot be associated with an interested party; cannot be, or previously have been, an employee of or affiliated with an interested party; nor can a trustee be a relative of an interested party.[46]

Adherence to these provisions limiting communication and who may serve as trustees is monitored by three different supervising ethics offices, one in each of the U.S. House of Representatives, the Senate, and the executive branch.[47]

B. *Qualified Blind Trust Antecedents*

The Ethics in Government Act's standardization of the elements and operation of blind trusts sprang from a history of sporadic and informal blind trust use among public officials. Briefly reviewing the history of government officials' use of blind trusts reveals that some of the problems prompting federal legislation have not been solved by the advent of qualified blind trusts. Specifically, early use of blind trusts may have originated from a desire to give the public appearance that a policymaker was avoiding conflicts of interest without actually blinding the policymaker to an asset that stood to influence the execution of official duties. Legislation establishing qualified blind trust rules has not solved this problem.

45. Telephone conversation with Katja Eichinger, Counsel, Senate Select Comm. on Ethics (Feb. 23, 2007). Because the initial assets are listed in the trust document itself, a public record, there is no obligation to report these assets on a public financial disclosure report annually. *See also* discussion *infra* notes 147–49 and accompanying text. Senator Frist, for example, knew that his blind trusts held HCA stock, yet he did not list these assets as belonging to the trust on his public financial disclosure statement. *See supra* notes 6–11 and accompanying text.

46. 5 U.S.C. app. § 102 (f)(3)(A)(i)(I)–(III) (2000).

47. Executive branch qualified blind trusts are monitored by the Office of Government Ethics. 5 U.S.C. app. § 109(18)(D). The office was established by the Ethics in Government Act of 1978. *Id.* § 401(a). Particular agencies, however, have individual administrative offices in charge of monitoring compliance with the financial disclosure mandate of the Ethics in Government Act within the agency. *See, e.g.*, U.S. GEN. ACCOUNTING OFFICE, GAO/GGD-90-51, GOVERNMENT ETHICS: HUD FINANCIAL DISCLOSURE REPORTS MISSING OR NOT REVIEWED (1990) (criticizing the Department of Housing and Urban Development's system for obtaining and reviewing financial disclosure statements). The legislative branch is monitored separately because the Constitution allows Congress exclusive authority to regulate itself. Costa, *supra* note 1, at 19. The House Committee on Standards of Official Conduct oversees qualified blind trusts for U.S. Representatives and House officers and employees. 5 U.S.C. § 109(18)(B). The Senate Select Committee on Ethics monitors qualified blind trusts Senators and Senate officers and employees. *Id.* § 109(18)(A).

President Lyndon B. Johnson appears to have been the first elected U.S. official to use a blind trust.[48] Nevertheless, Johnson knew about significant holdings in the trust.[49] When Johnson took office as Vice President in 1963, his family's ownership of a radio and television station in Texas deepened conflict of interest concerns that had followed him for nearly two decades. These concerns first arose when Johnson purchased a radio station while serving in the U.S. House of Representatives, then applied for a Federal Communications Commission ("FCC") license to construct a television station while serving as a U.S. Senator.[50] Johnson claimed he had not lobbied the FCC or cast a vote to further his media interests, but his political position likely played a role in securing favorable FCC decisions that helped his media holdings grow.[51]

Upon Johnson's ascent to the vice presidency, his staff encouraged him to sell his radio and television assets. He and his family were reluctant to do so. Instead, the Johnsons created a "blind trust" naming two business associates and family friends as the trustees and giving them complete discretion.[52] While the trust provisions governing blindness are not known, the lawyer who drafted the trust reported that he was unaware of any agreement between the Johnsons and the trustees not to sell shares of the media holdings.[53] Given that one of his trustees

48. Costa, *supra* note 1, at 18.

49. The blind trust was likely created during the Kennedy Administration to help several cabinet undersecretaries avoid conflicts of interest. *Id.* (reporting that Sheldon Cohen, a tax partner at the law firm of Arnold, Fortas & Porter, was asked to find a solution to the Kennedy cabinet officials' potential conflicts). Within months of Kennedy's taking office, Congress passed significant conflict of interest legislation governing the executive branch. Bribery, Graft, and Conflicts of Interest, Pub. L. No. 87-849, 76 Stat. 1119 (1962) (codified as amended at 18 U.S.C. § 208 (2000)). While the legislation itself did not specifically mention blind trusts, its prohibitions lent themselves well to the creation of blind trusts. The statute continues to prohibit certain executive branch employees from participating in a matter in which the employee or those close to the employee have a known financial interest. *See* 18 U.S.C. § 208(a) (2000) (prohibiting participation when the employee knows of financial interests of a spouse; minor child; general partner; organization in which the employee serves as an officer, director, trustee, general partner or employee; or any person or organization with whom the employee is negotiating or has any arrangement concerning prospective employment). *See also supra* notes 35–36, and accompanying text.

50. Costa, *supra* note 1, at 18; *see also* ROBERT DALLEK, LYNDON B. JOHNSON: PORTRAIT OF A PRESIDENT 52 (2004) (discussing the Johnsons' decision to purchase radio station KTBC and commenting that Johnson's "involvement in a business that largely depended on the actions of a Federal agency for its success created a clear conflict between his private interests and public position").

51. DALLEK, *supra* note 50, at 76–77.

52. Costa, *supra* note 1, at 18–19; ROBERT DALLEK, FLAWED GIANT: LYNDON JOHNSON AND HIS TIMES, 1961–1973, at 611 (1998).

53. Costa, *supra* note 1, at 19.

was the executive director of the Johnsons' broadcasting stations, Johnson must have had some degree of comfort that the trustees would not sell his interests.[54] Indeed, Johnson continued to own his radio and television properties when he left office in 1969.[55]

Guidelines on how to structure and use blind trusts emerged slowly on the federal level. Interestingly, these initial guidelines were more restrictive of the types of assets appropriate for a blind trust than is current federal law. The U.S. Department of the Interior, in 1975, may have been the first federal agency to formulate standards relating to blind trusts.[56] These standards required a trustee to divest holdings that created conflicts of interest, and prohibited the trustee from acquiring assets that might create a conflict of interest.[57]

In January 1977, President-elect Carter issued ethics guidelines in the aftermath of the Watergate scandal.[58] Carter's transition team proposed voluntary blind trusts for Carter appointees as an alternative to divestiture.[59] While Carter's guidelines limited blind trusts to cash or diversified assets, Carter himself placed his interests in two family-owned businesses into a trust that incorporated blind trust features.[60] Because Carter's trust prevented trustees from selling his share of a family farm, Carter continued to know of his ownership interest in that business.

---

54. Johnson's trustees were Donald S. Thomas, an Austin attorney and business associate, and Jesse Kellam, the executive director of the broadcasting stations that the Johnsons owned. DALLEK, *supra* note 52.

55. *Id.* Ironically, Johnson championed openness in government. In 1966, Johnson signed the Freedom of Information Act into law, stating: "This legislation springs from one of our most essential principles: a democracy works best when the people have all the information that the security of the Nation permits." Carolyn Bingham Kello, *Drawing the Curtain on Open Government? In Defense of the Federal Advisory Committee Act*, 69 BROOK. L. REV. 345, 346 n.7 (citing Steven Goldberg, Freedom Paper No. 6: Public Access to Government Information, http://usinfo.state.gov/products/pubs/archive/freedom/freedom6.htm (last visited Oct. 2, 2003)).

56. S. REP. NO. 95-639, at 3 (1978) [hereinafter SENATE BLIND TRUST REPORT].

57. *Id.*

58. *Id.* (citing *Texts of Carter Statement on Conflicts of Interest and Ethics; Appointees' Guidelines*, N.Y. TIMES, Jan. 5, 1977, at A17).

59. *Texts of Carter Statement on Conflicts of Interest and Ethics; Appointees' Guidelines*, N.Y. TIMES, Jan. 5, 1977, at A17.

60. *Id.* Carter transferred his interest in Carter's Warehouse and Carter Farms, Inc. to a trust that he may not have labeled a blind trust, but that limited information he could receive from his trustee. "No reports will be made to Jimmy Carter from the trustee or any investment advisors other than minimum tax information and an annual statement of the net value of the trust." *Id.* The trust agreement specified that the trust would retain Carter's interest in the farm, but would rent it for an annual fixed amount. Carter was to receive income from this interest not to exceed the amount established during 1977, to ensure that he and his family would not be affected from profits or losses of farm operations. Carter's partnership interest in Carter's Warehouse was to be either leased for four years for a fixed amount, or sold, at the discretion of the trustee. *Id.*

While both Presidents Johnson and Carter knew of the assets they held in trust, they may have been kept in the dark about management decisions. However, in most cases, blind management of sighted assets does not go far enough to foreclose the possibility that decisions could be tainted by a policymaker's interest in protecting known investments. Johnson, for example, may not have known of his radio and television stations' contractual commitments, but he did know that the health of his investments depended on FCC determinations and he was in a position in Congress and the White House to influence the FCC. Similarly, Carter stood to affect farm policy knowing of his family's agricultural interests, despite the fact that he may not have been involved in day-to-day decisions regarding his family farm.

Within months of the release of Carter's ethics guidelines, the Senate amended its Standing Rules to require dissolution of blind trusts existing in the Senate. The resolution established, as the sense of the Senate, that blind trusts should be either dissolved or modified to permit disclosure unless the Senate could establish a rule, or Congress pass legislation, that mandated minimum requirements and standards for blind trusts.[61] In other words, the Senate maneuver was intended to press for unified rules regulating the establishment of blind trusts. The Senate Committee on Governmental Affairs held hearings on blind trusts in June 1977.[62] Congress eventually enacted the Ethics in Government Act on October 26, 1978, which included rules governing qualified blind trusts.[63]

III. WHY BLIND TRUSTS FAIL TO DETER OR AVOID CONFLICTS OF INTEREST

A large part of why blind trusts fail to safeguard against conflicts of interest is because they operate contrary to traditional trust norms. To understand the faults of blind trusts, then, it is first important to understand how a traditional trust works as a financial management device.

---

61. S. Res. 110, 95th Cong. (1977) (resolving to amend Rule XLII of the Standing Rules of the Senate).

62. SENATE BLIND TRUST REPORT, *supra* note 56, at 8.

63. Ethics in Government Act of 1978, Pub. L. No. 95-521, 92 Stat. 1824 (1978).

A. Traditional Private Trusts Compared with Blind Trusts

A private trust is a legal arrangement under which a trustee manages property for one or more beneficiaries.[64] In a traditional trust, a grantor establishes the trust by conveying property to a trustee to manage for a person who is not willing or able to do so.[65] The trustee owns legal title to trust property and is held to a fiduciary standard of conduct.[66] As a fiduciary, the trustee must manage the trust property according to the interests of the beneficiaries. The trustee's actions are judged by an objective standard of care.[67]

Under this traditional version of a trust, a trustee must provide beneficiaries with enough information about the trust property and its management to enable beneficiaries to protect their interests.[68] Depending on the nature of the beneficiary's interest, a trustee usually has to provide an annual report of information related to the "trust property, liabilities, receipts, and disbursements, including the source and amount of the trustee's compensation, a listing of the trust assets and, if

---

64. Trusts are now commonly used for estate planning purposes, as well as for gratuitous transfers and management of property. When a grantor establishes a trust for estate planning purposes, state law does not require the grantor, trustee and beneficiary to be three separate parties. Rather, a grantor can avoid probate by conveying all of his assets into a revocable trust. The grantor is also the trustee and beneficiary during his lifetime, and the trust names a beneficiary to receive the trust's assets when the grantor dies. JESSE DUKEMINIER ET AL., WILLS, TRUSTS, AND ESTATES 485 (7th ed. 2005). As long as the trust names a beneficiary on the death of the grantor, courts have declared that the division of legal and equitable title is maintained even though the grantor retains the power to revoke the trust during his life. *E.g.*, Farkas v. Williams, 125 N.E.2d 600, 604 (Ill. 1955). This death-time beneficiary has an equitable interest in the trust; therefore the initial grantor owes the same fiduciary duty to this death-time beneficiary as would any trustee. *Id.* at 607–08.

65. Trusts were created in medieval England when grantors conveyed land to someone else to manage for the benefit of members of religious orders who had taken vows of poverty and were forbidden from owning property. GEORGE GLEASON BOGERT & GEORGE TAYLOR BOGERT, THE LAW OF TRUSTS AND TRUSTEES 11 (1965). Early trusts under feudalism were also used to avoid paying obligations owed to the lord of the manor. *Id.* Historically, trusts were useful primarily to convey property. Modern trusts are employed and valued as flexible asset management devices. *See, e.g.*, John H. Langbein, *The Contractarian Basis of the Law of Trusts*, 105 YALE L.J. 625, 629 (1995).

66. DUKEMINIER ET AL., *supra* note 64, at 490.

67. *Id.* at 490–91.

68. UNIF. TRUST CODE § 813 (2000) (amended 2005). A trustee does not need to furnish information to beneficiaries with "remote remainder interests." *Id.* § 813 cmt. The exact scope of fiduciary duties varies somewhat among the states. The Uniform Trust Code, completed by the Uniform Law Commissioners in 2000, has been adopted by nineteen states and the District of Columbia. The National Conference of Commissioners on Uniform State Laws, A Few Facts About the . . . Uniform Trust Code, http://www.nccusl.org/nccusl/uniformact_factsheets/uniformacts-fs-utc 2000.asp (last visited Mar. 9, 2007). *See also* RESTATEMENT (THIRD) OF TRUSTS § 82 (2005) (describing trustee's general duty to furnish information to beneficiaries).

feasible, their respective market values."[69] With this information, the beneficiary can monitor the extent to which a trustee is complying with fiduciary duties.[70]

The traditional trust exploits a beneficiary's self-interest while attempting to curb a trustee's self-interest. Only the beneficiary has a financial motive to scrutinize the trustee's performance and adherence to trustee standards. A trustee's erstwhile interest in usurping trust funds is counteracted by the liability that fiduciary law imposes on such wrongdoing.

Blind trusts try to replicate the asset management function of a traditional "sighted" trust without relying on a beneficiary to watch over the trustee. To the contrary, a blind trust operates against the self-interest of a beneficiary by forbidding the extensive reporting that the trustee of a traditional trust owes to beneficiaries. The "blindness" involved is that of the beneficiary, who is kept in the dark by the trustee about the identity and management of the trust assets. By definition, then, a blind trust alters the very element of a traditional trust that makes the instrument work as a means to allow one person to manage wealth for another.[71]

As a general proposition, there are two interrelated problems with using a blind trust to prevent conflicts of interest. First, because neither the trustee nor the beneficiary has sufficient incentive to keep the blindfold on, the trust may not actually prevent conflicts of interest. In a traditional private trust, a beneficiary's self-interest operates to ensure the trustee is complying with the trustee's duties. A blind trustee's duty to withhold information about the trust's investments, however, is not in the beneficiary's immediate self-interest.[72] To the contrary, the blind

---

69. UNIF. TRUST CODE § 813(c) (2000) (amended 2005); *see also* RESTATEMENT (THIRD) OF TRUSTS § 83 (2005) (describing trustee's duty to keep records and provide reports).

70. A beneficiary who is a minor child or incompetent adult will necessarily rely on a parent, guardian, or conservator to receive information from a trustee and monitor the trustee's compliance with fiduciary duties. *See supra* note 23.

71. A blind trust also resembles a modern revocable trust in that the grantor and the primary beneficiary are one and the same person. *See supra* note 64. It is, however, very different from a typical revocable trust. The grantor of a blind trust must relinquish control over his assets to an outside trustee, unlike a typical revocable trust grantor who often maintains control as trustee. In addition, the purpose of a revocable trust is probate avoidance rather than to manage assets for someone else, so the trustee's adherence to fiduciary duties becomes less important. *See supra* note 64.

72. Incentives or penalties established by law to regulate a blind trust can bring the maintenance of blindness more within a beneficiary's self-interest. Executive branch employees who knowingly participate in matters affecting their financial interests are subject to criminal sanctions. 18 U.S.C. § 208 (2000). Members of Congress may incur civil penalties for seeking prohibited information from a trustee. *See infra* notes 78–79 and accompanying text (discussing

trust's grantor *qua* beneficiary is likely very interested in keeping updated on the status and management of his assets. And it is this grantor turned beneficiary who selects and pays the trustee, and retains the right to revoke the trust. This could potentially affect the trustee's resolve to maintain the blindfold. Furthermore, without the flow of information regarding the management of the trust from the trustee to the beneficiary, the third party trustee becomes less accountable. The lack of trustee oversight may also tend to erode incentives for blindness. A trustee who wants to avoid an after-the-fact claim for breach of fiduciary duty may be inclined to share proscribed information regarding trust assets. Likewise, a grantor troubled by the lack of oversight may pressure a trustee for this prohibited information.

Second, the existence of a blind trust may appear to eliminate the possibility that a conflict of interest will arise for a policymaker, when it in fact does not. A blind trust does not automatically shield a policymaker from conflicts of interest, given that the policymaker knows the identity of the assets he initially placed in a blind trust, and may have restricted a trustee from transferring some of these assets.[73] Where a blind trust masks an actual or apparent conflict of interest, members of the public may think that a decision is impartial when it may in fact be tainted by a policymaker's knowledge and protection of his personal investments. Blind trusts, then, impair the openness of the decision-making process that is key to democratic governance.

B. Mechanisms to Substitute for a Beneficiary's Self-Interest

Qualified blind trust rules try to squelch a beneficiary's self-interested desire to seek information from a trustee and attempt to replace the valuable role this self-interest plays in scrutinizing a trustee's actions. The rules also establish a means of monitoring the flow of information, or lack thereof, between an interested party and a trustee.[74] For example, the qualified blind trust statute puts a supervising ethics office in charge of determining whether a trust arrangement meets the criteria for a qualified blind trust.[75] The supervising ethics office must also approve of a proposed trustee, presumably by ensuring that the

---

penalties).

73. *See* 5 U.S.C. app. § 102(f)(3)(B) (2000) (authorizing a supervising ethics office to approve a restriction on the transferability of an asset).

74. *See supra* note 37 and accompanying text (defining "interested party" as "a reporting individual, his spouse, and any minor or dependent child").

75. 5 U.S.C. § 102(f)(7)(C). *See also supra* note 47 and accompanying text (identifying three supervising ethics offices).

trustee meets the statutory criteria for being independent.[76] This same office is designated to receive copies of authorized written communications between an interested party and his trustee.[77] Finally, the Ethics in Government Act subjects a trustee and a reporting individual to civil penalties for attempting to take off the blindfold shielding the reporting individual from knowledge of his assets.[78] The Attorney General may bring a civil action against anyone who knowingly and willfully, or even negligently, discloses or solicits unauthorized blind trust information.[79] The bill initially passed by the Senate in 1977 authorized not only civil penalties, but also imprisonment for up to one year for knowing and willful violations.[80] The final version that Congress enacted in 1978, however, omitted criminal liability.[81]

A public official may have additional incentive to maintain blindness beyond the civil penalties provided for in the Ethics in Government Act. A policymaker's circumvention or violation of the blind trust rules could attract public criticism and result in the loss of a position or career. Moreover, separate legislation subjects executive branch employees to criminal liability for substantial and knowing financial conflicts of

---

76. *See supra* note 46 and accompanying text (discussing independence of trustee).

77. 5 U.S.C. §102 (f)(5)(E). *See supra* notes 40–42 and accompanying text (relating to authorized communication between an interested party and a trustee).

78. A trustee may not disclose unauthorized information to "an interested party," may not acquire assets prohibited by the trust instrument, may not solicit advice from an interested party regarding the trust if the trust instrument or the statute forbids doing so, and may not fail to file any document required to be filed by the statute. 5 U.S.C. § 102(f)(6)(A)(i)–(iv). A reporting individual may not "solicit or receive" unauthorized information regarding a qualified blind trust, nor fail to file any document required by the qualified blind trust rules. *Id.* § 102(f)(6)(B)(i)–(ii).

79. In an action regarding a knowing and willful violation, a court may not assess a penalty exceeding $10,000. *Id.* § 102(f)(6)(C)(i). In an action regarding a negligent violation, a court may not assess a penalty exceeding $5000. *Id.* § 102(f)(6)(C)(ii). This author has not been able to identify any civil actions brought by the Attorney General under these provisions.

80. SENATE BLIND TRUST REPORT, *supra* note 56, app. A at 33 (reproducing the qualified blind trust provisions of S. 555, 95th Cong. (1977), which would have imposed criminal sanctions in § 303(d)(6)(C)(i)).

81. Congress recently authorized imprisonment of not more than one year for any person who knowingly and willfully falsifies information that a person is required to report under 5 U.S.C. § 102, the Ethics in Government Act. Honest Leadership and Open Government Act of 2007, Pub. L. 110-81 § 702, 121 Stat. 735, 775–76, *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:publ081.110.pdf. This criminal penalty apparently applies not only to trust information included in a financial disclosure report, but to any document that must be filed with a supervising ethics office, including a trust document, a list of the assets initially transferred into the trust, a notice from a reporting individual that he has transferred a new asset into an existing blind trust, copies of written communication between a trustee and an interested party, and notification of the dissolution of a blind trust.

interest.[82] For the trustee, the statutory civil penalties may pale in comparison to liability for breaching fiduciary duties.[83]

C. *Flaws with Statutory Blindfold and Ameliorative Attempts*

The safeguards discussed above do not fully replace the oversight traditionally performed by a self-interested beneficiary. Consequently, public officials benefiting from blind trusts may have a strong impulse to seek prohibited trust information. Knowing that a trustee is independent and is not sharing proscribed information with a beneficiary does not ensure the trustee is living up to the trustee's fiduciary duties. Nor do quarterly reports of net cash value or gains and losses of a trust suffice to ensure that a trustee is complying with fiduciary obligations. This information does not guarantee a trustee is adhering to the duty of loyalty,[84] the prudent investor rule,[85] the duty to diversify trust assets,[86]

82. 18 U.S.C. §208(a) (2000). *See supra* note 49 (discussing the Bribery, Graft and Conflicts of Interest statute).

83. Under the Uniform Trust Code, a trustee is liable to the beneficiaries for violating trustee duties and may be compelled to redress a breach by "paying money, restoring property, or other means." UNIF. TRUST CODE § 1001(b)(3) (2000) (amended 2005).

84. The trustee's duty of loyalty is to "administer the trust solely in the interest of the beneficiaries." UNIF. TRUST CODE § 802(a) (2000) (amended 2005). The duty of loyalty precludes a trustee from, among other things, engaging personally in transactions involving trust property. UNIF. TRUST CODE § 802(a) (2000) (amended 2005); RESTATEMENT (THIRD) OF TRUSTS § 78(b) (2005). *See also* UNIF. PRUDENT INVESTOR ACT § 5 (1994) ("[T]rustee shall invest and manage the trust assets solely in the interest of the beneficiaries."). Forty-five states, the U.S. Virgin Islands, and the District of Columbia have adopted the Uniform Prudent Investor Act, which was approved by the Uniform Law Commissioners in 1994. The National Conference of Commissioners on Uniform State Laws, A Few Facts about the . . . Uniform Prudent Investors Act, http://www.nccusl.org/nccusl/uniformact_factsheets/uniformacts-fs-upria.asp, (last visited Aug. 23, 2007). *See also* RESTATEMENT (THIRD) OF TRUSTS § 78(a) (2005) (discussing duty of loyalty in the trustee and trust relationship).

85. The prudent investor rule requires the trustee to "invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust." UNIF. PRUDENT INVESTOR ACT § 2(a) (1994). While the rule has common law roots, it has been codified in the Uniform Prudent Investor Act and the Uniform Probate Code: the trustee has a duty to "observe the standards in dealing with the trust assets that would be observed by a prudent man dealing with the property of another . . . ." UNIF. PROBATE CODE § 7-302 (2005). The Restatement (Third) of Trusts also includes a prudent investor rule. RESTATEMENT (THIRD) OF TRUSTS § 90 (1990) (renumbered & amended 2005). Most states have enacted legislation governing a trustee's investment-related duties. *Prefatory Note*, UNIF. PRUDENT INVESTOR ACT, at 3–4 (1994).

86. UNIF. PRUDENT INVESTOR ACT § 3. The duty to diversify requires a trustee to see that assets comprise a broad, diversified portfolio, rather than allow investments to be concentrated in only a few industries or sectors of the economy. *Id.* § 3 cmt. at 29 (1994). The purpose of diversification is to reduce the risk of investing. *Id.*

rules governing proper delegation of trustee powers,[87] or the duty to keep "trust property separate from the trustee's own property."[88]

The qualified blind trust disclosure and communication restrictions would not necessarily shed light on a trustee in violation of one or more of these duties. For example, a trustee might improperly delegate to a family member the authority to invest sixty percent of the trust funds into fine art (violating the duty to diversify) that is hanging in the trustee's home (violating the duty of loyalty and the duty to keep trust property separate). Since the quarterly statements might not raise suspicion, the trustee's violation of these duties could remain unnoticed until the fine art market takes a turn for the worse, the trustee's home burns to the ground and the trust property is destroyed, or the trustee absconds with the art and is never heard from again. The purpose of a trustee's accounting obligation to a beneficiary is to enable a beneficiary to discover a breach of fiduciary duty before disaster strikes and the trust assets are lost.[89]

The model blind trusts disseminated by the Senate and executive branch try to plug this gap in trustee accountability by including a provision that requires the trustee to submit a full and complete financial accounting to the policymaker when a blind trust terminates.[90] This after-the-fact oversight may help ease the mind of a beneficiary. It may, however, present problems for a trustee, because it might encourage an

---

87. A trustee may delegate investment and management decisions as long as the trustee reasonably selects an agent, defines the scope and terms of delegation, and reviews the agent's decisions. *Id.* § 9(a)(1)–(3).

88. UNIF. TRUST CODE § 810(b) (2000) (amended 2005); RESTATEMENT (SECOND) OF TRUSTS § 179 (1959) (describing a trustee's duty to keep trust property separate from the trustee's own property).

89. Some trust law scholars maintain that fiduciary duties simply are default rules and that the grantor and trustee can agree by contract to waive them. *See, e.g.*, Langbein, *supra* note 65, at 629 (arguing that trustees' fiduciary duties find their origin in contract law); *see also* Melanie B. Leslie, *Trusting Trustees: Fiduciary Duties and the Limits of Default Rules*, 94 GEO. L.J. 67, 69 (2005) (pointing out that "[t]he default rule paradigm has increasingly influenced doctrine and permeates the recently promulgated Uniform Trust Code . . . .") (footnote omitted). Under a contractarian view of trusts, a grantor and trustee could privately agree to modify or waive application of some fiduciary rules. Others, however, argue against the ability to waive or significantly modify essential trustee duties. *Id.* at 69–70. Even if a policymaker could legally waive application of fiduciary duties, it seems highly unlikely that he would be willing to do so with no ability to monitor the trustee's performance.

90. Senate Select Comm. on Ethics, Sample Trust Agreement art. 15 (Oct. 7, 1994), http://ethics.senate.gov/downloads/pdffiles/trust.pdf [hereinafter Senate Sample Trust Agreement] (last visited Sept. 16, 2007); Office of Gov't Ethics, Model Qualified Blind Trust Provisions art. 17 (Mar. 2002 draft), http://www.usoge.gov/pages/forms_pubs_otherdocs/fpo_files/forms/frmodel_f38.pdf [hereinafter OGE Model Blind Trust] (last visited Sept. 16, 2007). This requirement is not part of the Ethics in Government Act, nor does it appear in the regulations governing executive branch blind trusts.

assessment of the trustee's performance from a superior position of hindsight. Whether a trustee has complied with fiduciary duties, particularly investment-related duties, is supposed to be "determined in light of the facts and circumstances existing at the time of a trustee's decision or action and not by hindsight."[91]

Blindness may be easier for trustees who have no proclivity to discuss investment decisions with a beneficiary. Nonetheless, the reporting individual has power over the trustee that may be sufficient to persuade a trustee to divulge information proscribed by the Ethics in Government Act. The reporting individual is the person who selects the trustee and the person who pays the trustee's fees. In addition, the reporting individual can seek to remove the trustee or can simply revoke the trust.

The threshold for trustee removal is not specified in the statute, but is set forth in vague terms in the regulations that govern executive branch blind trusts.[92] The Ethics in Government Act requires supervising ethics offices to approve only trustee selection, not trustee removal.[93] Executive branch regulations and the model blind trust instruments from supervising ethics offices permit a trustee to be substituted "upon a showing of necessity and appropriateness."[94] A trustee's interest in retaining the policymaker's business may erode resolve to keep investment data undisclosed if a beneficiary is pressuring for information.

---

91. UNIF. PRUDENT INVESTOR ACT § 8 (1994).

92. Executive branch qualified blind trusts operate under a set of administrative regulations that do not govern legislative qualified blind trusts. 5 C.F.R. §§ 2634.401–409 (2007).

93. 5 U.S.C. app. § 102(f)(3)(D) (2000).

94. 5 C.F.R. § 2634.405(e) (2007) ("The terms of a qualified trust may not be revoked or amended, except with the prior written approval of the Director, and upon a showing of necessity and appropriateness."). The Senate Sample Trust Agreement states that "[a]ny amendment of the terms of this Trust Agreement, including the appointment of a substitute or successor Trustee, shall require the prior written approval [o]f the Committee, upon a showing of necessity and appropriateness unless it relates to the testamentary provisions of this trust." Senate Sample Trust Agreement, *supra* note 90, art. 18. The executive branch Model Qualified Blind Trust Provisions includes nearly identical language. OGE Model Blind Trust, *supra* note 90, art. 20. There apparently is no established standard by which to measure "necessity and appropriateness." Telephone conversation with Katja Eichinger, counsel, Senate Select Comm. on Ethics (Feb. 23, 2007). Interestingly, this express authorization to replace a trustee appears to be relatively new. The Office of Government Ethics' Model Qualified Blind Trust Provisions, dated November 1, 1980, does not include such a provision. Instead, this earlier version allows revocation or amendment to the terms of the trust agreement with prior written approval, upon a showing of necessity and appropriateness—omitting the clause specifically relating to "the appointment of a substitute or successor Trustee." Office of Gov't Ethics, Model Qualified Blind Trust Provisions art. 1(B) (Nov. 1, 1980 draft), *reprinted in* FEDERAL ETHICS HANDBOOK E-83 (1981).

Because blind trust rules do not sufficiently compensate for the lack of oversight by the beneficiary over his trustee found in a traditional sighted trust, blind trusts may not actually avoid conflicts of interest, given the powerful incentive for a beneficiary to seek information on his assets. Moreover, the rules do not address the fact that the existence of a blind trust may lead public observers to believe that policymakers are indeed avoiding conflicts, when this might not be the case. The rules leave a significant gap inasmuch as misleading public comments can suggest a blind trust is truly blind when it might not be. Senator Frist took advantage of this gap by stating publicly that he did not know whether his blind trusts held HCA stock, when he had good reason to know that they did.[95]

The statutory efforts to maintain blindness, to provide oversight and to impose penalties for violations are not sufficient to overcome the problems inherent in blind trusts. Blindness runs contrary to the way most owners treat their property. An owner of property has a natural tendency to seek information on the health and management of an investment, particularly when the welfare of the owner or someone close to the owner depends on the investment. This natural tendency might be particularly strong for a newly-elected member of the House, who would be relinquishing power over his assets for what might only be a two-year term.

IV. RECOMMENDATIONS

A. *Full Disclosure Coupled with Recusal or Divestiture*

The best solution to the inadequacies of blind trusts is to eliminate their use as an exception to financial disclosure. Complete disclosure should be the rule. As Justice Louis Brandeis remarked, "sunlight . . . is the best of disinfectants."[96] The idea that openness of the democratic process leads to accountability is the entire premise behind requiring financial disclosure.[97] It also comports with the recent trend to enhance

95. *See supra* notes 9–10 and accompanying text.

96. "Publicity is justly commended as a remedy of social and industrial diseases. Sunlight is said to be the best of disinfectants; electric light the most efficient policeman." LOUIS D. BRANDEIS, OTHER PEOPLE'S MONEY 92 (1932).

97. The Senate Report on the Ethics in Government Act lists five rationales supporting public financial disclosure. Among them are that disclosure will increase public confidence in government and will enable the public to judge the performance of public officials. S. REP. NO. 95-170, at 21–22 (1978), *reprinted in* 1978 U.S.C.C.A.N. 4216, 4237–38.

and enforce disclosure in campaign finance law and with regard to policymakers' interaction with lobbyists.[98]

Requiring officials to disclose the identity of their financial interests on public financial disclosure forms puts the burden on the public to discover a potential conflict of interest. Once financial interests are disclosed and a potential conflict brought to light, a policymaker could present evidence that no conflict is posed, seek a waiver from conflict of interest rules, divest himself of the interest, or recuse himself from official decision-making related to the private interest.[99]

The policymakers who initially formulated the qualified blind trust favored disclosure and considered blind trusts extraordinary. The Senate Committee on Governmental Affairs, charged with drafting blind trust standards, recommended that "[f]or most government officials," conflicts of interest were best avoided by "financial disclosure, together with the divestiture or liquidation of those holdings . . . [creating] potential conflicts . . . or recusal from decisionmaking in matters where the outcome may materially affect the financial interests of the individual or his family . . . ."[100] The Committee expressly stated that it did not recommend blind trusts for all government officials.[101]

98. Bipartisan Campaign Reform Act of 2002, Pub. L. No. 107-155, 116 Stat. 81 (2002). The act furthered the interests of disclosure by banning national parties and federal candidates from raising "'soft money' ([previously] unregulated contributions to political parties or committees)." Audra L. Wassom, *Campaign Finance Legislation: McCain-Feingold/Shays-Meehan—The Political Equality Rationale and Beyond*, 55 SMU L. REV. 1781, 1790 (2002). *See also* Honest Leadership and Open Government Act of 2007, Pub. L. 110-81, 121 Stat. 735, *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:publ081.110.pdf (strengthening the Lobbying Disclosure Act).

99. Charles D. Fox & David A. Herpe, *Blind Trusts: Easing the Burdens of Government Service*, TR. & EST., Mar. 1993, at 28, 28–30.

100. SENATE BLIND TRUST REPORT, *supra* note 56, at 12.

101. *Id.* Blind trusts may not be as extraordinary as initially anticipated. According to the Senate Office of Public Records, the number of senators who maintain blind trusts tends to fluctuate between fifteen and twenty. Telephone Conversation with Pamela Gavin, Pub. Records Superintendent, Senate Office of Pub. Records (Feb. 23, 2007). As of February 2006, "in addition to Frist, 17 senators and several members of the House" used blind trusts. Costa, *supra* note 1, at 19. The same number applied as of February 2007. Telephone conversation with Pamela Gavin, Pub. Records Superintendent, Senate Office of Pub. Records (Feb. 23, 2007). The exact number of blind trusts in use in the House of Representatives and the executive branch is unknown. The House of Representatives Clerk's Office, which houses public documents, would not count the number of blind trusts in use within the House and suggested the author could visit the Legislative Resource Center to perform her own count. Telephone conversation with Janice Glosson, Registration and Compliance Clerk, Legislative Res. Ctr., Office of the Clerk, U.S. House of Representatives (Mar. 6, 2007). When the author attempted to perform a count of House blind trusts in person, the Legislative Resource Center ("Center") provided a list of names under the heading "Blind Trust Agreements." Center staff said the list, a 2005 tally of blind trusts among members of the House, was the most recent one available. The list showed that only nine blind trust agreements "still remain active." Incredibly, however, six of the nine members had retired before 2005, the Honorable Peter Hoagland having retired a full decade earlier. Interview with Janice Glosson,

Disclosure, coupled with alternative actions once a potential conflict arises, is not a trouble-free solution for a variety of reasons. Disclosure itself can be problematic. It may deter qualified individuals from seeking public office or contributing to government service. Disclosure may invite frivolous claims of conflicts that impair governance. A more extreme possibility is that an opponent or opportunist could use financial information to sabotage an official's financial welfare or even threaten family members. The Ethics in Government Act implicitly recognizes these possibilities and declares it unlawful for any person to obtain or use a financial disclosure report for any unlawful or commercial purpose, other than commercial use by media for dissemination to the general public.[102]

Further, even if the disclosure hurdle is cleared, the options for dealing with a potential or actual conflict will not always be easy to apply. In some instances, it may not be feasible for an official to recuse himself as often as the circumstances might require to avoid conflicts of interest. For example, high-level White House employees with diversified investment portfolios who participate in decisions affecting an array of industries could be asked to recuse so frequently that their ability to govern would be impaired. Furthermore, U.S. Senators and Representatives cannot be compelled to disqualify themselves from voting on matters related to their outside financial holdings.[103] The House of Representatives Ethics Manual explains that recusal is disfavored because it results in "the disenfranchisement of a Member's entire constituency on particular issues."[104] Presumably, financial disclosure operates to deter official decision-making on matters in which a member of Congress has a private financial interest because of the specter of being voted out of office. Despite a Congressional policy against abstention, recusal was presented as a viable alternative to blind trusts in debates before the enactment of current qualified blind trust rules.[105]

Registration and Compliance Clerk, Legislative Res. Ctr., Office of the Clerk, U.S. House of Representatives, in Wash., D.C. (Apr. 26, 2007). The list is on file with the author.

102. 5 U.S.C. app. § 105(c)(1) (2000). The Act further authorizes the Attorney General to "bring a civil action against [anyone] who obtains or uses a report" for a prohibited purpose. *Id.* § 105(c)(2).

103. SELECT COMMITTEE ON ETHICS, UNITED STATES SENATE, SENATE ETHICS MANUAL 124 (2003); HOUSE ETHICS MANUAL, *supra* note 3, at 153.

104. *See* HOUSE ETHICS MANUAL, *supra* note 3, at 157. Senator Frist is reported to have "rejected suggestions" that he recuse himself from consideration of health-care legislation because of his HCA investments. Jube Shiver, Jr., *Frist's Possible Conflicts Seen As No Problem Under Senate Rules*, L.A. TIMES, Dec. 22, 2002, at A27.

105. SENATE BLIND TRUST REPORT, *supra* note 56, at 8, 11 (summarizing testimony from the June 7 and 9, 1977 hearings of the Senate Committee on Governmental Affairs). Senator John

Divestiture also is not a certain cure. Its efficacy as a solution to financial conflicts of interest is limited, depending on the employee's duties. An employee cannot be expected to divest himself of all assets to avoid all financial conflicts. Doing so may present a hardship, particularly if the sale results in significant capital gains tax liability or the interest is a partnership or family corporation.[106] Tax laws can be amended to minimize capital gains tax liability, but there is no remedy to a forced divestiture of family-held financial interests.[107] Under a complete disclosure regime, a person holding financial interests that pose a conflict with official duties, for which both recusal and divestiture is impracticable, may be forced to forgo government service.

Executive branch employees have an additional, albeit limited, option if full disclosure reveals the existence of a conflict of interest. Under the Bribery, Graft, and Conflicts of Interest statute, an executive branch employee may seek a waiver of conflict of interest rules and be exempt from liability for acting in an official capacity while affected by a personal financial interest.[108] A conflict of interest may be waived only for very narrow reasons, one being the employee's financial interest is not substantial enough to affect the integrity of that employee's official duties.[109] Waivers, however, can be time consuming for the official who must explain the financial interest implicated and the conflict that it poses with his duties.

B. Alternative: Reform Blind Trust Legislation

Many policymakers and observers may consider complete financial disclosure an extreme solution to guarantee that a policymaker's financial interests do not affect governmental decisions. Because of the difficulties and risks associated with financial disclosure, it is likely that the blind trust will continue to operate as an exception to disclosure.

If blind trusts remain an alternative to complete disclosure, the qualified blind trust rules must be amended to strengthen their ability to

---

Durkin advocated that senators be required to disqualify themselves from participating in any vote on any issue in which the senator or a family member had a direct financial interest. *Id.* at 11. Currently, recusal from participation in a matter is the most common form of Ethics Agreement seen in the executive branch. REVIEWER'S REFERENCE, *supra* note 31, at 5-4.

106. Fox & Herpe, *supra* note 99, at 30.

107. A witness at the Senate hearings on blind trusts, Alan Morrison, Director of Litigation, Public Citizen, suggested postponing capital gains tax liability incurred as a result of divestiture. SENATE BLIND TRUST REPORT, *supra* note 56, at 11.

108. 18 U.S.C. § 208(b)(1) (2000).

109. *Id.* The legislative history reflects an intent to allow waivers for interests of "insignificant proportions." S. REP. NO. 87-2213, *reprinted in* 1962 U.S.C.C.A.N. 3852, 3863.

deter conflicts of interest. The remainder of this section proposes fortification of four different areas of blind trust operation and enforcement: 1) the rules regarding initial assets must be modified to ensure that these assets are converted to a form of investment not disclosed to beneficiaries; 2) the system of selecting and monitoring trustees must be changed to minimize a beneficiary's incentive to remove the blindfold and monitor a trustee's performance; 3) a trust beneficiary's financial disclosure requirements must be broadened to facilitate public oversight of potential conflicts of interest; and 4) additional penalties must be imposed for rule violations to further solidify blindness and boost public confidence in blind trusts. These ideas are intended to be a starting place for a larger debate on the appropriate scope and operation of blind trusts.

Taken together, these proposals will help address the two significant flaws of blind trusts. First, reforming qualified blind trusts will better allow the device to actually prevent conflicts because the blindfold will be in place more securely. Second, public watchdogs will have sufficient information about a policymaker's blind trust to know when it is truly blind. In other words, a policymaker will not be able to hide behind the shield of a blind trust when he knows the identity of the assets held in his trust.

Critics might argue that the proposed modifications will do little to actually prevent conflicts of interest in Congress because legislators need not abstain from decision-making when a conflict arises. Even if it becomes public knowledge, for example, that a lawmaker knows the identity of an asset in his qualified blind trust, the legislator cannot be compelled to abstain from decision-making, nor can he be required to request that a trustee dispose of the asset.[110] Nonetheless, these modifications will facilitate public oversight of potential conflicts. Legislators can forecast closer scrutiny and more public pressure should they continue to hold assets that pose frequent conflicts with official duties. Accordingly, these modifications may, in fact, prevent conflicts from occurring, at least when a legislator plans to seek reelection.

Furthermore, the only other option to actually prevent conflicts in Congress would be to require blind trusts for legislators who cannot recuse themselves when faced with a conflict of interest. Compulsory blind trusts for legislators, under the following proposed amended rules, would indeed be more effective as a means of avoiding conflicts.

---

110. *See supra* note 103 and accompanying text. Instructing a trustee to sell an asset that creates a conflict of interest is one of the statutorily authorized subjects of communication. 5 U.S.C. app. § 102(f)(3)(C)(vi) (2000).

However, requiring lawmakers to transfer their assets into blind trusts, along with those of spouses and dependent children, would likely discourage too many qualified candidates from considering public office.

1. Modify Rules Related to Initial Assets

A blind trust is only truly blind once the trustee transfers the initial assets out of the trust and replaces them with investments that the trustee is forbidden from disclosing to the reporting individual. Congress should consider four changes to current qualified blind trust rules to ensure that a reporting individual will, indeed, become blind to the initial assets and that this blindness will occur within a reasonable time after the trust's creation.

First, the rules should limit the type of financial interests that a grantor can place in a blind trust, so that holdings initially deposited are cash or easily transferable assets.[111] Requiring that a trust be funded solely with these types of readily marketable interests will allow a trustee to convey them out of a trust and reinvest the proceeds into new assets unknown to the reporting individual. Partnership interests, closely held family corporations, certain real estate holdings—assets that the reporting individual truly does not want to or is unable to transfer—should not be allowed to be held in a blind trust.[112] This limitation should also apply to any assets that a reporting individual transfers into a qualified blind trust after it is established. Assets that are not readily marketable are not appropriate for blind trusts and should be subject to financial disclosure obligations.[113]

Current blind trust rules already recognize the value of transferring only diversified assets to a blind trust. If a policymaker establishes a blind trust with a "well-diversified portfolio of readily marketable

---

111. This was one of President Carter's initial criteria for blind trusts, set forth in his January 1977 ethics guidelines. *Texts of Carter Statement on Conflicts of Interest and Ethics; Appointees' Guidelines*, N.Y. TIMES, Jan. 5, 1977, at A17. Alaska statutes authorize blind trusts for some public officials to limit their financial disclosure obligations. Alaska's rules do, however, limit the type of assets that may be transferred into the trust. Before 2007, the requirement was only that the assets "shall be marketable." ALASKA STAT. § 39.50.040(b)(1) (2004). Recent legislation expands this rule to prohibit, among other assets, "assets with permanency that makes transfer by the trustee improbable or impractical." Act of July 9, 2007, ch. 47, sec. 57, § 39.50.040(b)(1), 2007 Alaska Adv. Legis. Serv. 47 (LexisNexis).

112. Alaska's current statute gives a similar list: "real estate, security interests in personal property, mortgages, and interests in closely held businesses." *Id.*

113. *See* SENATE BLIND TRUST REPORT, *supra* note 56, at 5 (suggesting that a blind trust with "holdings [which] are likely to remain unchanged . . . is hardly a blind trust. It is nothing more than a management device.").

securities," then the reporting individual does not need to treat the initial trust assets as a financial interest for purposes of conflict of interest rules.[114] Furthermore, the trustee does not need to notify the reporting individual when any of these initial assets are transferred out of the trust.[115] Nonetheless, a reporting individual currently is not required to restrict blind trust interests to such diversified holdings.

Second, Congress should require a trustee to sell initial assets that may pose a conflict of interest as soon as is practicable after a reporting individual identifies the potential conflict.[116] Assuming that the first suggestion to limit initial blind trust holdings to easily transferable assets or cash is followed, a speedy sale of some initial trust property should pose no problem.

Third, blind trust rules should require trustees to turn over a certain percentage of the initial assets within a particular time frame to create more immediate blindness.[117] For example, within the first year of the trust's existence, a trustee could be required to transfer and reinvest at least sixty percent of the initial assets. A turn-over requirement is particularly feasible if the initial assets are limited to readily transferable investments, as suggested above. Trustees may be more comfortable operating under a mandatory sale rule if they are given safe harbor from the application of prudent investor rules.[118] While it might not be prudent for a trustee of a traditional private trust to turn over such a large percentage of initial assets, trustees compelled to do so under revised qualified blind trust rules should be shielded from liability.

Finally, a reporting individual should never be allowed to restrict a trustee's power to transfer a particular asset. Qualified blind trust rules currently allow an official to instruct a trustee not to sell an inception asset, as long as the supervising ethics office approves of the restriction.[119] Accordingly, a new qualified blind trust can include assets that the trustee cannot transfer, so the reporting individual will continue to know the identity of these holdings. Assets over which a policymaker

---

114. 5 U.S.C. app. § 102(f)(4)(B)(i)(I) (2000).

115. *Id.* § 102(f)(4)(B)(i).

116. This was part of the Department of the Interior's regulations regarding blind trusts for its employees, effective July 1975. SENATE BLIND TRUST REPORT, *supra* note 56, at 3 (citing 43 C.F.R. § 20.735.24(a)(3)).

117. Witnesses suggested this idea during the Senate Committee hearings in 1977, but Congress apparently rejected it as an arbitrary way of monitoring blind trusts. *Id.* at 10 (summarizing testimony from the June 7 and 9, 1977, hearings of the Senate Committee on Governmental Affairs).

118. *See supra* note 85 and accompanying text (discussing the trustee's duty to manage trust assets as a prudent investor).

119. 5 U.S.C. app. § 102(f)(3)(B) (2000).

wishes to maintain ownership should be disclosed rather than protected by the appearance of blindness. A trustee of a blind trust must have complete discretion to dispose of any trust asset.

These proposals may give rise to the same capital gains tax liability problems identified in the earlier discussion on divestiture. Again, if a reporting individual must divest low tax basis assets so that only diversified assets remain in a blind trust, or a trustee must sell low tax basis property to adhere to these new rules, capital gains tax rules may need to be amended.[120]

2. Strengthen Trustee and Blind Trust Monitoring

A number of modifications can be made to qualified blind trust rules to strengthen compliance, improve the way a trustee's performance is monitored, and enhance the independence of a trustee. These include establishing an independent government body to supervise blind trust creation and administration or delegating such supervisory responsibility to a private entity; authorizing only trustees selected from a slate of preapproved institutional trustees; disclosing the name of blind trustees on financial disclosure reports; assigning trustee monitoring responsibility to an independent entity or to the Attorney General; and clarifying the standards for trustee removal.

To ensure compliance with limits on communication and proper disclosure, the statute should be amended to change the way blind trust rules are supervised. The current supervisory system raises concern for at least two reasons. First, low staff levels cause worry about the viability of managing current oversight duties. Three separate offices now oversee federal qualified blind trusts.[121] These minimally-staffed offices[122] also manage other types of ethics issues for their institutions, such as oversight of lobbying disclosure rules.[123] Among the staffs'

---

120. SENATE BLIND TRUST REPORT, *supra* note 56, at 11.

121. *See supra* note 47 (identifying supervising ethics offices).

122. The House Committee on Standards of Official Conduct employs eight staff attorneys. Committee Staff, http://www.house.gov/ethics/CommitteeStaff.htm (last visited Mar. 14, 2007). The Senate Select Committee on Ethics staff includes four attorneys. JOINT COMM. ON PRINTING, U.S. CONGRESS, CONGRESSIONAL DIRECTORY 375 (Sept. 2006 online rev.), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_congressional_directory_interim_sep06&docid=109thin_txt-63.pdf. The executive branch Office of Government Ethics, Office of General Counsel and Legal Policy employs sixteen staff attorneys, program analysts, and others. U.S. Office of Government Ethics, http://www.usoge.gov/pages/about_oge/staff_directory.pdf (last visited Aug. 16, 2007).

123. The jurisdiction of the House Committee on Standards of Official Conduct is described at http://www.house.gov/ethics/CommitteeJurisdiction.htm (last visited Oct. 21, 2007); the scope of the

other duties, these offices are responsible for reviewing and approving all qualified blind trust instruments, initial trustee appointments, and amendments to trusts, and for reviewing all written communications between policymakers and the trustees of their blind trusts.[124]

The practicality of small staffs, particularly in Congress, to manage significant oversight duties has troubled even some legislators. Legislators recently have introduced bills to create an independent Office of Public Integrity to supervise Congress's compliance with ethics rules, after a number of lobbying scandals indicated lax oversight on the part of the House and Senate ethics committee staffs.[125] The initial 2006 proposal ultimately failed,[126] but lawmakers have since introduced new bills to establish an independent monitoring body, showing that questions about committee oversight capacities remain.[127]

The second concern with current blind trust oversight relates to whether ethics staffs can watch over the institutions that support them. Skeptics might challenge the efficacy of charging staff with overseeing ethics rules within their own institutions. Staff members are employed at the will of each of the three institutions, yet they are responsible for monitoring compliance with ethics rules and investigating alleged

Senate Select Committee on Ethics is illustrated at http://ethics.senate.gov/ (last visited Oct. 21, 2007); the functions of the various subdivisions within the executive branch Office of Government ethics are explained at http://www.usoge.gov/pages/about_oge/organ_functions.html (last visited Oct. 21, 2007)

124. 5 U.S.C. app. §§ 102(f)(3)(D), (f)(5)(E) (2000). Blind trust instruments can be lengthy. The executive branch's Office of Government Ethics issued Model Qualified Blind Trust Provisions that totaled seventeen pages, excluding an appendix that lists initial assets. OGE MODEL BLIND TRUST, *supra* note 90.

125. *See, e.g.*, H.R. 4799, 109th Cong. §§ 1, 3 (2006), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_cong_bills&docid=f:h4799ih.txt.pdf (proposing an independent Office of Public Integrity that would have oversight of, among other things, financial disclosure and other reports filed by all members of Congress pursuant to the Ethics in Government Act of 1978); S. 2259, 109th Cong. § 2 (2006), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_cong_bills&docid=f:s2259is.txt.pdf (proposing an Office of Public Integrity only for oversight of Senate ethics matters). The Center for Public Integrity charged that in the Senate alone, nearly 14,000 lobbying documents that should have been filed were missing and that nearly 300 individuals and entities lobbied without registering. Alex Knott & Sam Stein, *Senate Rejects Office of Public Integrity*, CENTER FOR PUBLIC INTEGRITY, Mar. 28, 2006, http://www.publicintegrity.org/report.aspx?aid=791.

126. *See* Sheryl Gay Stolberg, *Senate Approves Lobbying Limits by Wide Margin*, N.Y. TIMES, Mar. 30, 2006, at A1 (reporting on Senate approval of a lobbying reform bill, but rejection of a proposed Office of Public Integrity).

127. *See, e.g.*, H.R. 422, 110th Cong. (2007), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:h422ih.txt.pdf (proposing to establish an Office of Public Integrity "as an independent office within the legislative branch of the Government, to reduce the duties of the Committee on Standards of Official Conduct of the House of Representatives and the Select Committee on Ethics of the Senate, and for other purposes"). Similar to its predecessor bill, this proposal would delegate to an independent office oversight of financial disclosure and other reports filed pursuant to the Ethics in Government Act of 1978. *Id.* § 3(a)(1).

violations. In some cases, the supervising ethics staff themselves might be required to submit financial disclosure statements and opt to establish blind trusts to limit their required disclosures.[128]

These concerns can be addressed by amending the statute to create one independent body whose sole task is to oversee all qualified blind trusts. Such an entity might be structured as an independent agency similar to the Federal Election Commission, which is charged with administering federal campaign finance law.[129] Alternatively, oversight of blind trust rules could be delegated to a private entity. Privatizing this function poses a hurdle no more significant than has privatization of other government jobs.[130] Any number of trust companies or accounting firms would likely be qualified and willing to contract to monitor blind trusts.[131]

In addition to assigning blind trust supervision to an independent body, the rules imposing blindness might be enhanced by exerting more control over trustee selection and making the identity of a trustee public. The rules could require that policymakers select trustees from a slate of institutional trustees qualified and pre-approved to serve as blind trust fiduciaries. The executive branch qualified blind trust regulations already take a step towards this end by requiring that trustees be

---

128. *See supra* note 28 and accompanying text (referring to congressional employees required to report financial interests). In Senate debates over a proposed Official Code of Conduct, Senator Goldwater proclaimed that "the American people will not be fooled by an in-house procedure which leaves it up to the Members of Congress to police themselves." 123 CONG. REC. 10,044, 10,054 (1977) (statement of Senator Barry Goldwater on proposed Senate Resolution 110, Official Code of Conduct). While the 1978 Ethics in Government Act codified some of the rules the Senate voluntarily imposed on itself, the Act leaves monitoring of blind trusts in the hands of each institution.

129. Congress created the Federal Election Commission ("FEC") in 1974 in an amendment to the Federal Elections Campaign Act. Pub. L. No. 93-443, § 208(a), 88 Stat. 1279–86 (1977) (codified as amended at 2 U.S.C. § 437c (2000)). The Commission is composed of six members who are appointed by the President and confirmed by the Senate. 2 U.S.C. § 437c(a)(1) (2000). Former outside counsel to two prior Speakers of the U.S. House of Representatives recently suggested an independent monitoring body similar to the FEC as a means of regulating the conduct of lobbyists. Randy Evans, *Follow That Lobbyist*, N.Y. TIMES, Feb. 10, 2007, at A15.

130. That is not to say that privatization of public education, prisons, subsidized housing, health care, welfare, and other government services has been without censure. *See, e.g.*, Gillian E. Metzger, *Privatization as Delegation*, 103 COLUM. L. REV. 1367 (2003) (discussing constitutional problems with government use of private entities to implement government programs); Mark Calaguas, *Military Privatization: Efficiency or Anarchy?*, 6 CHI.-KENT J. INT'L & COMP. L. 58 (2006), http://www.kentlaw.edu/jicl/articles/spring2006/s2006_Mark_Calaguas.pdf (last visited Aug. 13, 2007) (addressing concerns with the use of private military contractors).

131. The House Committee on Standards of Official Conduct has made a practice of recruiting accounting professionals from the General Accounting Office to assist in reviewing financial disclosure reports. U.S. GEN. ACCOUNTING OFFICE, GAO/GGD-89-103, FINANCIAL DISCLOSURE: LEGSLATIVE [sic] BRANCH SYSTEMS IMPROVED BUT CAN BE FURTHER STRENGTHENED 31 (1989).

institutions rather than individuals.[132] Limiting potential trustees to carefully selected institutional entities could help to ensure that policymakers select trustees with resolve to maintain the blindness.

The reporting individual should also be required to disclose the name of the trustee on each year's public financial disclosure report. Currently, a reporting individual need not do so. In theory, the overseeing ethics office maintains a copy of the trust document naming the trustee. However, that information currently is available to the public only upon specific request and payment of a processing fee.[133] While identifying a trustee on each year's financial disclosure report would not directly enhance the monitoring of a trustee, doing so could bring more public or peer pressure on trustees to adhere to blind trust rules and fiduciary duties. For example, watchdogs concerned about the independence of a trustee could determine whether the trustee appears on an elected reporting individual's list of campaign contributors.

Additional modifications should be made to monitor trustee performance in managing trust property. No individual or institution systematically examines whether a trustee is complying with fiduciary duties.[134] The lack of such oversight creates incentive for a reporting individual to carry out his own oversight and seek more information from a trustee than is authorized by the Ethics in Government Act.

An independent oversight body like the two alternatives proposed above could also be made responsible for overseeing trustee compliance with fiduciary duties. Alternatively, trustees could be required to provide complete accountings to the Attorney General's office. This approach is similar to the way trustees of tax-exempt charitable trusts are

---

132. 5 C.F.R. § 2634.406(a)(2) (2007). Alaska also requires that the trustee of a blind trust be "a bank, trust company, or other institutional fiduciary." Act of July 9, 2007, ch. 47, sec. 57, § 39.50.040(b)(2), 2007 Alaska Adv. Legis. Serv. 47 (LexisNexis).

133. Document retention and purging policies make some original trust documents unavailable to the public. *See supra* note 101 and accompanying text. The Honest Leadership and Open Government Act of 2007 requires the Clerk of the House of Representatives to post on its Internet site reports that members of the House are required to file "under section 103(h)(1) of the Ethics in Government Act of 1978." Honest Leadership and Open Government Act of 2007, Pub. L. 110-81 § 304, 121 Stat. 735, 752–53, *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:publ081.110.pdf. Section 103(h)(1) refers to "reports required under this title [Financial Disclosure Requirements of Federal Personnel]." 5 U.S.C. app. § 103(h)(1) (2006). Because a trust instrument likely is not a "report," a trust will probably not be included in the documents that the Clerk must post.

134. Trustees managing qualified blind trusts for executive branch officials, however, must maintain and make available for inspection by the Office of Government Ethics ("OGE") the trust's books of account and other records. 5 C.F.R. § 2634.403(b)(11) (2007). There is no requirement that OGE staff actually inspect such records.

monitored.[135] Members of Congress, however, would likely balk at granting trustee monitoring authority to the Department of Justice.[136]

Finally, blind trust rules should be amended to bolster the long-term independence of trustees. For example, regardless of whether qualified blind trusts continue to be supervised by current ethics offices or by a new independent body, the oversight entity should have the authority to investigate possible violations of trust restrictions and determine that a trust no longer meets the requirements of a qualified blind trust based on violations.[137] Moreover, qualified blind trust rules should be clear on the standard of proof necessary for trustee removal. Mechanisms need to be in place to ensure that a reporting individual does not remove a trustee simply because the trustee refused to disclose unauthorized information related to the trust assets. Specifically, the standard should be tied to the performance of the investments and whether a trustee is following any general investment guidelines established by the reporting individual.

3. Expand Disclosure of Blind Trust Assets to Promote Citizen Oversight

Additional changes should be made to facilitate public oversight of potential conflicts of interest. Because a reporting individual apparently is not required to report on each financial disclosure statement the identity of assets known still to be in the trust, citizen oversight is extraordinarily cumbersome. The rules should require reporting individuals to list on their annual financial disclosure statements any asset held by a qualified blind trust that they know is still in the trust.

One of the significant innovations of the 1978 Ethics in Government Act authorizing blind trusts is that it refused to consider assets that the grantor initially placed in the trust to be truly blind.[138] Prior blind trusts

135. Most states have adopted statutes authorizing the state's Attorney General to enforce charitable trusts, but others have established this duty through judicial decisions. MARION R. FREMONT-SMITH, GOVERNING NONPROFIT ORGANIZATIONS: FEDERAL AND STATE LAW AND REGULATIONS 305–07 (2004). The problem of enforcing a charitable trust is analogous to concerns regarding oversight of a trustee's actions under a blind trust. Because the beneficiaries of a charitable trust are the public at large, there is no specific person to function like the self-interested beneficiary of a private trust. *Id.* at 301. Accordingly, the government, represented by the Attorney General, exercises oversight of charitable trusts by invoking its *parens patriae* power. *Id.*

136. While likely to present political problems, this idea may not pose a separation of powers problem because the Attorney General would be monitoring the trustees rather than monitoring an independent branch of government.

137. For executive branch qualified blind trusts, the Office of Government Ethics has such investigatory power, as well as the power to revoke the certification of a trust as a qualified blind trust. 5 C.F.R. § 2634.503 (2007).

138. SENATE BLIND TRUST REPORT, *supra* note 56, at 13.

were deemed blind the day after the trust was established despite the fact that the trust obviously contained the same investments placed in it by the government official.[139] Instead, the new rules required the grantor to disclose the initial assets to a supervising ethics office, which would then be subject to public scrutiny.[140]

This treatment of initial assets continues. Policymakers who establish qualified blind trusts must submit to the supervising ethics office a list of the assets initially transferred into the trust, along with the category of the asset's value (not the actual value).[141] These lists of initial blind trust assets are available to the public on request.[142] Apparently, however, the public official need not disclose the identity of these known assets on an annual financial disclosure form.[143] Because the list of initial assets is a public record, there is no obligation to specifically identify them on a public financial disclosure report annually.[144] When a trustee sells all or most of an initial asset, he must notify the public official and the supervising ethics office of the assets sold, unless all of the initial assets were well-diversified.[145] These notices of sale are also available to the public.[146]

Thus, in order for a citizen to determine whether a policymaker has a potential conflict of interest where a blind trust is involved, the citizen first must request, and likely pay a fee to obtain, a financial disclosure statement, from which he learns that a policymaker has established a blind trust.[147] It does not, however, indicate whether all of the

---

139. *Id.*

140. *Id.* at 14.

141. 5 U.S.C. app. § 102(f)(5)(A)(ii) (2000).

142. *Id.* § 102(f)(5)(D).

143. *See supra* notes 6–8, 11, 45 and accompanying text. Senator Frist knew that his blind trusts held HCA stock, yet did not list these assets as belonging to the trust on his financial disclosure report. In fact, Senator Frist maintained on his public financial disclosure form that he did not know the identity of the underlying assets held by his blind trusts. *See supra* notes 6–8, 11.

144. Telephone conversation with Katja Eichinger, Counsel, Senate Select Comm. on Ethics (Feb. 23, 2007).

145. 5 U.S.C. §§ 102(f)(3)(C)(iii), 102(f)(4)(B)(i).

146. *Id.* § 102 (f)(5)(D).

147. The cost of Senator Frist's 2006 Financial Disclosure Statement was $5.00. Watchdog organizations have posted some older forms on the Internet, but these might not reflect any amendments that a reporting individual made to those forms. According to the Senate Office of Public Records, each page copied and produced is twenty cents. Telephone conversation with Pamela Gavin, Pub. Records Superintendent, Senate Office of Pub. Records (Feb. 23, 2007). House of Representatives disclosure forms and some blind trust documents may be printed directly from a database located at the Legislative Resource Center for ten cents a page. Author visit to Legislative Res. Ctr. (Apr. 26, 2007). The Honest Leadership and Open Government Act of 2007 requires that financial disclosure reports of Members of the House be posted on the Clerk's website beginning no later than August 1, 2008. Honest Leadership and Open Government Act of 2007, Pub. L. 110-81 §

individual's assets initially placed in the trust have been sold or otherwise disposed of. For this information, a citizen must request, and pay to obtain, the list of assets initially placed in the trust. While this process may be direct in some instances, blind trust agreements that include a list of initial assets are purged after six years from the House of Representatives public data base.[148] Finally, the citizen must request all of the trustee's reports of assets that have been transferred out of the trust for every year the blind trust has existed, again paying a fee for every record obtained. Even with all of this information, a citizen does not know whether the trust holds assets that the supervising ethics office has authorized the trustee to keep in the trust.[149]

Requiring annual disclosure of known blind trust assets would more completely fulfill the spirit of the statutory mandate that an initial asset "shall be considered a financial interest of the reporting individual, for the purposes of any applicable conflict of interest statutes, regulations, or rules of the Federal Government (including section 208 of title 18, United States Code), until such time as the reporting individual is notified by the trustee that such asset has been disposed of, or has a value of less than $1,000."[150] To treat the asset as a "financial interest" would be to disclose its identity annually, as required for other financial interests.[151] Annual disclosure would comport more closely with the way

---

304, 121 Stat. 735, 752–53, *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:publ081.110.pdf.

148. The Legislative Resource Center, under the auspices of the Office of the Clerk of the U.S. House of Representatives, maintains publicly available documents for the House. This author visited the Legislative Resource Center and was not able to retrieve certain blind trust documents from that office because they had been destroyed, pursuant to a policy to purge financial disclosure documents after six years. Interview with Janice Glosson, Registration and Compliance Clerk, Legislative Res. Ctr., Office of the Clerk, U.S. House of Representatives, in Wash., D.C. (Apr. 26, 2007).

149. A citizen could identify that a restricted asset remains in the trust by comparing the list of initial assets and the notices of sale subsequently received in the ethics office. But simply knowing that the trust retains an asset is not enough information to determine whether the asset poses a conflict of interest. The fact that the reporting individual specifically sought to keep the asset in the trust may raise a more significant specter of a conflict. The policymaker's attachment to the asset might point to a potential conflict of interest regarding a related decision.

150. 5 U.S.C. § 102(f)(4)(A).

151. At least one state that authorizes the use of blind trusts to avoid public financial disclosure requires annual disclosure of initial assets remaining in the trust. California requires public officials to disclose investments and interests in real property, as well as the value category and sources of income. CAL. GOV. CODE §§ 87200–87203 (West 2005). An interest in a blind trust need not be disclosed "if those interests or investments are acquired by the trustee *after* the trust complies with subsection (b)." CAL. CODE REGS. tit. 2 § 18235(a) (2000) (emphasis added). Section (b) requires that a blind trust be established with a disinterested trustee with complete discretion who is prohibited from disclosing information "concerning the replacement assets." Tit. 2 § 18235(b)(1)–(4) (2000). The California Fair Political Practices Commission further clarifies that "you must disclose reportable assets originally transferred into the blind trust and income from those original

in which the original drafters of the qualified blind trust rules envisioned that these initial assets would be treated. Indeed, the Senate report on the Ethics in Government bill states that, "[d]uring that transition [between the time a trust is established and the time a trustee transfers the initial assets], the public interest in knowing that financial conflicts of interests do not exist *is satisfied by financial disclosure*."[152]

Citizen oversight would also be enhanced if the Ethics in Government Act was amended to reflect a more functional approach to the identification of people who must comply with financial disclosure obligations.[153] Currently, the Ethics in Government Act requires that an official compelled to disclose financial assets must also include those of his spouse and dependent children.[154] This group of individuals is too narrow. No disclosure is required, for example, for dependent parents or parents-in-law, or unmarried partners. Consequently, the financial interests of these individuals need not be disclosed despite the fact that such interests may impair a policymaker's impartial judgment.

The circle of those required to report should be broadened to include "dependents and members of a reporting individual's immediate family," not just a spouse or dependent child. Alaska's statutes governing standards of conduct define "immediate family" in a manner that would more securely identify financial conflicts, and could be applied to federal officials required to disclose their financial interests. In Alaska, a person's "immediate family" includes a spouse or domestic partner.[155] "Immediate family member" encompasses parents, children (including stepchildren and adopted children) and siblings who reside with, are financially dependent on, or share a substantial financial interest with the person.[156]

---

assets until they have been disposed of by the trustee." CAL. FAIR POLITICAL PRACTICES COMM'N, 2006/2007 FORM 700 STATEMENT OF ECONOMIC INTERESTS REFERENCE PAMPHLET 15 (2006), *available at* http://www.fppc.ca.gov/forms/700-06-07/refpamphlet06-07.pdf.

152. SENATE BLIND TRUST REPORT, *supra* note 56, at 14 (emphasis added).

153. Specifically, §§ 102(e)(1), (f)(1), (f)(2)(C), and (e)(3) of Title 5 app. of the U.S. Code should be amended.

154. 5 U.S.C. app. § 102(e)–(f) (2000).

155. ALASKA STAT. § 24.60.990(a)(6)(A) (2004). A "domestic partner" is a "person who is cohabiting with another person in a relationship that is like a marriage but that is not a legal marriage." ALASKA STAT. § 24.60.990(a)(5) (2004). Alaska, however, does not require everyone in a policymaker's "immediate family" to disclose financial information. Instead, certain policymakers, their spouses or domestic partners, dependent children, and (for legislators) nondependent children living with the policymaker must disclose. Act of July 9, 2007, ch. 47, sec. 43, § 24.60.200, 2007 Alaska Adv. Legis. Serv. 47 (LexisNexis) (governing legislators); ALASKA STAT. § 39.50.030 (2004) & Act of July 9, 2007, ch. 47, secs. 55, 56, §§ 39.50.030(b), (h), 2007 Alaska Adv. Legis. Serv. 47 (LexisNexis) (governing judicial officers and the executive branch).

156. ALASKA STAT. § 24.60.990(a)(6)(B) (2004).

Some might reason that the entire purpose for blind trusts is to absolve citizens of monitoring responsibilities. In theory, the blind trust is a replacement for citizen oversight. From this perspective, it should not matter if monitoring is difficult. Nonetheless, because an official with a blind trust knows the identity of his initial assets and the assets a trustee is prevented from transferring, some outside monitoring is still in order, as the situation with Senator Frist's HCA stock illustrates. Requiring annual disclosure of assets that a reporting individual knows to be held in a blind trust will facilitate citizen oversight, as will taking a more realistic approach to determining who must comply with reporting duties.

4. Impose Additional Penalties

Enhancing the penalties related to violating blind trust rules will strengthen the blindness provisions and discourage policymakers from inappropriately hiding behind a blind trust that may not truly be blind. Blind trust rules should impose a fine on a reporting individual who publicly issues a statement disavowing knowledge of assets held in a blind trust when the individual knows or has reason to know of those assets. The current Ethics in Government Act authorizes civil and criminal sanctions against anyone who knowingly and willfully falsifies a financial disclosure report.[157] The Act, however, does not penalize reporting individuals for publicly misrepresenting their knowledge of assets held by a blind trust. The absence of a penalty for such misrepresentation allows a reporting individual to perpetuate the myth of blindness even though the underlying initial assets are still quite visible to the policymaker.[158]

It is possible that such false statements could already be considered unlawful under the federal statute criminalizing false statements.[159] However, while the statute has been applied to false statements made on

157. Civil penalties are authorized under 5 U.S.C.S. app. § 104(a) (LEXIS through Pub. L. 110-83 (Sept. 20, 2007)). The recent Honest Leadership and Open Government Act of 2007 added a criminal sanction. *See supra* note 81.

158. *See, e.g.*, public statements that Senator Frist made, *supra* notes 9–10 and accompanying text.

159. 18 U.S.C. § 1001 (2000). To constitute a violation, the false statement made directly or indirectly to the government must relate to "any matter within the jurisdiction of the executive, legislative, or judicial branch of the Government of the United States." § 1001(a). "Jurisdiction is bestowed by any statutory basis for the agency's access to the information and is present wherever a false statement relates in some way to a matter in which a federal agency has the power to act." Jennifer L. Kraft & David A. Sadoff, *Ninth Survey of White Collar Crime: False Statements*, 31 AM. CRIM. L. REV. 539, 559–60 (1994) (footnote omitted).

a financial disclosure report,[160] it might be a stretch to apply it to a policymaker's statement to the press regarding his knowledge (or lack thereof) of assets held in a blind trust that is reported on a financial disclosure report. If this false statements statute would not apply, the elements of a fraudulent misrepresentation claim could track those of the Restatement (Second) of Torts § 526.[161]

Given the strong incentive to remove the blindfold from blind trust beneficiaries, the Ethics in Government Act should also include criminal liability for a trustee or reporting individual's knowing and willful violation of blind trust rules related to disclosing or seeking information. The draft ethics bill approved in 1977 by the Senate did call for criminal sanctions of up to one year imprisonment for a knowing and willful violation.[162] Congress eliminated this in the final version passed in 1978.[163] The specter of criminal liability would strengthen the resolve of a trustee and reporting individual to comply with qualified blind trust rules seeking to limit the flow of information between them.[164] Moreover, adding a criminal penalty would be consistent with Congress's recent bolstering of civil and criminal penalties for other ethics rules violations.[165]

---

160. *See, e.g.*, United States v. Espy, 989 F. Supp. 17, 23 (D.D.C. 1997), *rev'd in part on other grounds*, 145 F.3d 1369 (D.C. Cir. 1998) (violation of Ethics in Government Act by making false statements on financial disclosure was basis for criminal charges under 18 U.S.C. § 1001).

161. The Restatement (Second) of Torts states:

> A misrepresentation is fraudulent if the maker (a) knows or believes that the matter is not as he represents it to be, (b) does not have the confidence in the accuracy of his representation that he states or implies, or (c) knows that he does not have the basis for his representation that he states or implies.

RESTATEMENT (SECOND) OF TORTS § 526 (1977).

162. *See supra* note 80 and accompanying text.

163. However, criminal liability follows where an *executive branch* employee has a conflict of interest and there is a "causal link between [the] particular Government matter in which the employee participates and [the] effect on the [employee's] asset or other interest (direct effect)." There must be a "*real possibility of gain or loss* as a result of development in or resolution of that matter (predictable effect)." REVIEWER'S REFERENCE, *supra* note 31, at 5-1 (citing United States v. Gorman, 807 F.2d 1299, 1303 (6th Cir. 1986); 5 C.F.R. §§ 2635.402, 2640.103).

164. Congress recently added a criminal sanction for any person who knowingly and willfully falsifies information required under the Ethics in Government Act reporting obligations of § 102. *See supra* note 81. While this will deter false assertions on documents that a trustee and reporting individual must file, it will do nothing to deter unauthorized communication.

165. The Honest Leadership and Open Government Act of 2007 increased civil fines and added criminal sanctions for failure to comply with lobbying disclosure requirements. Honest Leadership and Open Government Act of 2007, Pub. L. 110-81 § 211, 121 Stat. 735, 749, *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_public_laws&docid=f:publ0 81.110.pdf. Similarly, it increased civil fines and added a criminal penalty for knowing and willful falsification of information an individual is required to report under § 102 of the Ethics in Government Act. *Id.* § 702, 121 stat. at 775–76.

V. CONCLUSION

Policymakers began to use blind trusts as a means of avoiding full disclosure, in some instances, of assets that a policymaker was unwilling to divest. The lack of uniform standards governing blind trusts compelled Congress to debate the device's merit and conclude that it was valuable if properly regulated. Thirty years of regulation under the Ethics in Government Act is sufficient to determine whether blind trusts adequately insulate governmental decisions from decision-makers' financial interests. While blind trusts may allow some individuals with wealth and privacy concerns to engage in public service when they might otherwise have been discouraged from doing so by financial disclosure rules, the potential loss of integrity in decision-making does not counterbalance this advantage. Perhaps it is time to place more value on the sanctity of the decision-making process and determine if full disclosure unacceptably sacrifices a broad pool of talented public servants. In the interim, while this alternative approach is debated, Congress must strengthen the qualified blind trust rules so that the device can deter financial conflicts of interest and enhance public confidence in the integrity of decision-making.

286

***

PROJECT ON GOVERNMENT OVERSIGHT

April 18, 2022

The Honorable Zoe Lofgren
Chairperson, Committee on House Administration
House of Representatives
1309 Longworth House Office Building
Washington, DC 20515

The Honorable Rodney Davis
Ranking Member, Committee on House Administration
House of Representatives
1216 Longworth House Office Building
Washington, DC 20515

Dear Chairperson Lofgren and Ranking Member Davis:

Thank you again for affording the Project On Government Oversight (POGO) the opportunity to testify today, and thank you for holding a hearing on the important issue of congressional stock trading. As laid out in POGO's testimony, we urge Congress to act immediately to ban members, their immediate families, and their senior staffs from trading stocks.[1] But understanding that transformational reforms take time in Congress, we also wanted to take this opportunity to lay out what POGO would encourage Congress to consider next — a much stricter ban that applies to Congress and across government.

A law with government-wide applicability should permit officials to invest in diversified mutual funds (including diversified exchange-traded funds) and Treasury bonds, but should prohibit most other investments. The law should apply to all elected and politically appointed officials in the federal government's three branches, as well as to a limited number of career officials in specified top executive positions.[2] Consistent with existing practice for presidential appointees to Senate-confirmed positions in the executive branch, divestiture would be required within 90 days of an individual commencing service in a covered position.[3]

Several narrow exceptions could apply. The law could exempt personal residences; interests in a spouse's employer; family farms; defined benefit pension plans in any employer; diversified

[1] POGO has called for passage of a congressional stock trading ban that merges the best elements of the TRUST in Congress Act (H.R. 336), the Ban Congressional Stock Trading Act (S. 3494), and the Bipartisan Ban on Congressional Stock Ownership Act of 2022 (H.R. 6678; S. 3631).
[2] We do not recommend including all public financial disclosure filers in these new restrictions, as that population includes medical doctors and others who have no supervisory authority. *See* 5 U.S.C. app. § 101(f)(3).
[3] 5 C.F.R. § 2634.802(b).

Project On Government Oversight
1100 13th Street NW, Suite 800
Washington, DC 20005
202.347.1122
info@pogo.org
www.pogo.org

mutual funds held in any employer-sponsored retirement plans; any other type of diversified investment funds held in an employer-sponsored fund, provided that the plan is managed by an independent trustee; any holding of a federal, state, or local government retirement plan, provided that the holding is not an interest in an individual company; and qualified tuition plans (529 plans). Cash equivalents, such as money market mutual funds or certificates of deposit, could also be exempted from the prohibition on ownership. The prohibition would not cover automobiles, artwork, and other personal property.

There should be specific provisions addressing divestitures to prevent covered officials from gaming the system. The law should provide that a sale in exchange for a note, such as an I.O.U. note, does not qualify as a divestiture. Likewise, a sale or gift to a "discretionary trust" should not qualify as a divestiture if the employee, their spouse, or their minor child is an eligible recipient.[4] In the case of any sale to a relative or a trust for the benefit of a relative, the law should require the employee to make full public disclosure of the terms of the sale, including sale price, method and timing of payment, and all other terms or conditions. The law should also include a public disclosure requirement for employees who ever reacquire the asset by gift, purchase, inheritance, or other means, even if they do so after leaving the government. Finally, the law could grant slightly longer deadlines, such as 180 days instead of 90 days, to divest private investment funds; however, the divestiture requirement should not be extended further or lifted merely because an employee has outstanding capital commitments (because, after all, the employee made the choice to go into government).

Exceptions for certain family trusts can be granted to avoid forfeiture of an investment portfolio, but only in the case of executive branch officials who are subject to the conflict of interest law 18 U.S.C. § 208, which includes a recusal framework to manage the potential conflict. Officials in the legislative and judicial branches are not subject to the recusal requirement under the criminal conflict of interest law; therefore, there is no way to manage any conflicts of interest created by a family trust and should not be exempted for those officials.[5]

This family trust exception should be extremely narrow to address only trusts that are truly beyond the control of the employee. Therefore, the exception should apply only when all of the following conditions are met:

1. The trust is irrevocable.
2. The grantor of the trust is not the employee, their spouse, their minor child, or a trust for the benefit of any such person.

---

[4] The Office of Government Ethics defined the term "discretionary trust" in a legal advisory. Office of Government Ethics, "Discretionary Trusts," Legal Advisory DO-08-024, August 6, 2008, https://www.oge.gov/Web/oge.nsf/Legal%20Docs/F24E8762B7CBAFCE852585BA005BECCA/$FILE/DO-08-024.pdf?open.

[5] If Congress wanted to create an exception for certain family trusts, it could require that members recuse from any deliberations or votes on legislation affecting interests held in those family trusts. While that would deprive their constituents of a voice in Congress, their constituents would have the option of voting for a candidate who has not chosen to be sidelined by conflicts of interest. Any such recusal requirement should commence at the beginning of a new term, so that constituents have the option to vote out any members who refuse to put the public's interest first. Alternatively, Congress could, at least, restrict members from committee assignments likely to give rise to conflicts of interest related to their personal financial interests.

3. No property or money has been contributed to the trust by the employee, their spouse, or their minor child.
4. No property or money has been contributed to the trust by another trust that would not meet the standard established in this section.
5. The trust was established either:
   a. prior to this law becoming applicable to the employee; or
   b. upon, or incident to, the death of a person.
6. Neither the employee nor their spouse or minor child has any control over the holdings of the trust or power to replace the trustee.
7. The employee or their spouse has submitted a written request to the trustee that covered investments be divested and has received either a negative response or no response at all.

For any permissible trades, such as purchases and sales of diversified mutual funds or the exercise of stock options in a spouse's employer, the official should be subject to a requirement to file an irrevocable notice of the trade not less than 45 days before the trade. The notice should be released publicly online on the 46th day after filing. All covered officials, including judges, should also be subject to the requirement to file a periodic transaction report. The law could also impose a blackout period on trading by Members of Congress, their spouses, and their minor children while Congress is in session, excluding pro forma sessions.

Several reforms are needed specifically for judicial branch officials. Judges and Supreme Court justices should be required to file public statements articulating their reasons for recusing or declining to recuse from cases. They should be subject to an absolute ban on any outside earned income or royalties, including from book sales and teaching. They should also be subject to the criminal conflict of interest law 18 U.S.C. § 208. Moreover, the Supreme Court should be required to adopt a code of ethical conduct.

Transparency and enforcement with respect to all requirements applicable to top government officials should be greatly enhanced. All covered executive branch officials, including White House appointees, and senior congressional staffers should be required to sign ethics agreements identifying the steps they will take to avoid conflicts of interest. The supervising ethics offices for all three branches should be required to put in writing and to post online all of the following records pertaining to covered officials: ethics agreements, certifications of ethics agreement compliance, requests for certificates of divestiture, certificates of divestiture, screening arrangements, qualified blind trust agreements, qualified blind trustee notices of sales, advance notices of trades, financial disclosure reports (including periodic transaction reports),[6] ethics waivers, written notices of the acceptance of gifts that are given by prohibited sources or because of one's official position,[7] and all ethics-related approvals and authorizations.[8] To ensure that

[6] We are not advocating that the disclosures of all 26,000 public filers in the executive branch be posted online, only those filed by elected officials, political appointees, and senior congressional staffers.
[7] The Office of Government Ethics has defined the term "prohibited source" at 5 C.F.R. § 2635.203, and we would add lobbyists to this definition. We would not, however, require disclosure of gifts from a spouse, relative, or fiance.
[8] POGO also has a proposal for a database of executive branch ethics records that we would be happy to share on request.

officials remain willing to seek ethics advice however, Congress should not require the online posting of records of individual advice and counseling provided by ethics officials.

The executive branch ethics program should be enhanced by granting full branch-wide investigative authority to an office that must conduct investigations at the request of the director of the Office of Government Ethics (OGE). The investigative office should be one that already has both investigative authority and an adequately resourced, experienced staff to conduct meaningful investigations. One option would be to create an executive branch-wide inspector general with ordinary investigative and audit responsibility over all executive branch programs and officials (excluding the president and the vice president) that are not currently subject to the jurisdiction of an inspector general, with supplemental ethics jurisdiction over the rest of the executive branch (again, excluding the president and vice president) upon request of OGE's director.[9] Another option might be to assign this investigative authority to the Special Counsel of the U.S. Office of Special Counsel.

Whoever receives the investigative authority, however, the authority should only be to investigate and write a factual report; it should not include authority to recommend a decision. Having two different offices opine on whether a violation occurred could weaken enforcement if the two offices were to disagree, and only OGE possesses the necessary expertise to consider the application of government ethics laws and regulations. Finally, Congress should rescind subsection (f) of OGE's organic statute, which unreasonably hampers the office's ability to enforce government ethics requirements.[10] In its place, Congress should substitute language authorizing the office to request an investigation, consider an employee's written or oral response, and either drop the matter or prosecute the employee before the Merit Systems Protection Board (MSPB), which should have the authority to impose penalties.

The MSPB should have the authority to impose stiff penalties on political appointees in the executive branch, and its decisions should be subject only to limited judicial review. Penalties for noncompliance with a requirement to divest an asset could include either total forfeiture of the asset or a significant percentage of the value of the asset, as well as a civil monetary penalty. For other violations, penalties would include only civil monetary penalties proportional to the seriousness of a violation of OGE's regulations. A decision by the MSPB could be appealed to the Court of Appeals for the Federal Circuit. As is currently the case for appeals from final decisions of the MSPB, however, the court should conduct only a limited review circumscribed by statute.[11]

These recommended reforms would greatly strengthen the government ethics program. We emphasize again, however, that pursuing these reforms should occur after Congress moves quickly to enact a congressional stock trading ban.

[9] The Campaign Legal Center made a similar proposal with which we agree, except that POGO believes the investigator should have no authority to decline to conduct an investigation upon receipt of a request of the Director. Walter Shaub, "Policy Proposals on Ethics," Campaign Legal Center, November 9, 2017, https://campaignlegal.org/document/walter-shaub-policy-proposals-ethics.

[10] 5 U.S.C. app. § 402.

[11] 5 U.S.C. § 7703.

Thank you again for the opportunity to provide POGO's perspective on this important issue. My colleagues and I remain ready and willing to assist in your efforts however we can.

Sincerely,

Liz Hempowicz
Director of Public Policy

Walter Shaub
Senior Ethics Fellow

NATIONAL TAXPAYERS UNION

April 7, 2022

The Honorable Zoe Lofgren
Chair, Committee on House Administration
1309 Longworth House Office Building
Washington, D.C. 20515

The Honorable Rodney Davis
Ranking Member, Committee on House Administration
1216 Longworth House Office Building
Washington, D.C. 20515

Dear Chair Lofgren, Ranking Member Davis, and Members of the Committee:

On behalf of National Taxpayers Union (NTU), the nation's oldest taxpayer advocacy organization, I write to thank you for holding your April 7 hearing, "Examining Stock Trading Reforms for Congress."[1] This is an important public policy matter that affects the nation's taxpayers – who pay the salaries of Members of Congress – and the entire institution of Congress.

I would like to reiterate NTU's support for two proposals to prohibit Congressional stock trading: the TRUST in Congress Act (H.R. 336) from Reps. Abigail Spanberger (D-VA) and Chip Roy (R-TX),[2] and the Ban Congressional Stock Trading Act (S. 3494) from Sens. Jon Ossoff (D-GA) and Mark Kelly (D-AZ).[3] NTU has supported the TRUST in Congress Act since its first introduction in June 2020.[4] We continue to applaud the leadership of Rep. Spanberger, Rep. Roy, Sen. Ossoff, and Sen. Kelly for leading legislation to restore and rebuild the trust that Congress has lost, over many years and controversies, with constituents and voters.

Some Congressional leaders have attracted attention for their rejection of legislation to limit or prohibit stock trading by Members of Congress and their spouses, with one leader claiming that stock trading reflects a "free market" economy where lawmakers can participate.[5] We accept the premise of this claim – that America is a free market economy – but reject the notion that Members of Congress are mere average participants in that economy. There are at least two major categories of privileges afforded Members of Congress that make them (and, by extension, their spouses) far different from the average "free market" participant:

---

[1] Committee on House Administration. "Examining Stock Trading Reforms For Congress." Retrieved from: https://cha.house.gov/committee-activity/hearings/examining-stock-trading-reforms-congress (Accessed April 4, 2022.)
[2] Congress.gov. (Introduced January 15, 2021.) "H.R.336 - TRUST in Congress Act." Retrieved from: https://www.congress.gov/bill/117th-congress/house-bill/336/ (Accessed April 4, 2022.)
[3] Congress.gov. (Introduced January 12, 2022.) "S.3494 - Ban Congressional Stock Trading Act." Retrieved from: https://www.congress.gov/bill/117th-congress/senate-bill/3494 (Accessed April 4, 2022.)
[4] Representative Chip Roy. "Rep. Chip Roy On TRUST In Congress Act." June 15, 2020. Retrieved from: https://roy.house.gov/media/press-releases/rep-chip-roy-trust-congress-act (Accessed April 4, 2022.)
[5] Slodysko, Brian. "Pelosi defends lawmaker stock trades, citing 'free market.'" *Associated Press*, December 15, 2021. Retrieved from: https://apnews.com/article/business-nancy-pelosi-congress-8685e82eb6d6e5b42413417f3d5d6775 (Accessed April 4, 2022.)

1) Members of Congress have access to privileged information, often before the general public, on a wide variety of topics, including national security and public health, that could affect the price of individual stocks or the performance of entire stock indices; and
2) Members of Congress have a unique ability to actually impact the performance and price of individual companies' stocks through their votes, proposals, and, often, their powers on Congressional committees.

For these reasons, at the very least, we believe that Members of Congress and their spouses should not be able to trade individual stocks during a Member's term of service and for some short time after their service (specifically, 180 days in H.R. 336 and S. 3494).

This legislation from Reps. Spanberger and Roy, and Sens. Ossoff and Kelly, also provides reasonable accommodations for Members of Congress in the implementation of such restrictions, such as allowing Members to place existing assets in a qualified blind trust (rather than requiring divestment) and allowing them to own widely held assets like mutual funds that track the broad performance of a stock index. These accommodations broadly align with NTU's philosophy on Congressional stock trading: we wish to prevent Members of Congress from financially benefiting from their taxpayer-funded privileges in a manner disproportionate to the average investor, but we understand that many Members of Congress might like to participate in market- or index-wide gains that benefit tens of millions of other investors from a variety of socioeconomic backgrounds.

Overall, NTU strongly believes that the TRUST in Congress Act and the Ban Congressional Stock Trading Act strike an appropriate balance between protecting the public trust for taxpayer-funded work and ensuring public service requirements are not so unreasonable as to prevent citizens from engaging in public service. Both pieces of legislation are worthy of bipartisan support, and we urge the Committee to consider these bills as soon as practicable.

More broadly, we urge Congress to continue working on this issue in a bipartisan and bicameral manner, rather than turning this pressing matter into a political football between the two major parties. True, lasting reform on Congressional stock trading will require the support of both chambers of Congress and both parties. American taxpayers will not be convinced that any new law regarding Congressional stock trading was passed in good faith if one political party uses the legislation to unilaterally attack the other party. We believe Reps. Spanberger and Roy have shown Congressional leadership the way forward in advancing a strongly bipartisan product.

Thank you for your consideration of NTU's work on the issue of Congressional stock trading, and we appreciate the Committee's interest in this matter. Should you have any questions, or if you would like to discuss these proposals with us further, I am at your service.

Sincerely,

Andrew Lautz
Director of Federal Policy

CC: Members of the Committee on House Administration

122 C Street NW, Suite 650 * Washington, DC 20001 * Phone: (703) 683-5700 * Fax: (703) 683-5722 * ntu.org

Congress of the United States
Washington, DC 20515

April 7, 2022

The Honorable Zoe Lofgren
Chair
Committee on House Administration
1309 Longworth House Office Building
Washington, D.C. 20515

Dear Chairwoman Lofgren,

We write to you to propose certain changes to the Ban Conflicted Trading Act (H.R. 1579), to be made in Committee, and we respectfully request that this letter and the attached amended bill text be submitted into the record during the hearing on this subject to be held by the Committee on House Administration on April 7, 2022. Additionally, we request a staff-level meeting to discuss these proposed changes.[1]

Based on conversations with advocates, subject-matter experts, and Members and staff of the Committee on House Administration, we propose certain changes to the Ban Conflicted Trading Act, which address a wide variety of issues and concerns, closing potential loopholes and ensuring the original intent of the legislation will be accurately reflected in its legal interpretation and implementation. The scope of financial instruments now available to investors is broad and growing. As a result, the choices facing the Committee in regulating Members' investments are also extensive and complicated. In the interest of collaborating constructively, we propose the following changes to address some of these issues.

The amended text would cover Members' spouses and dependents under the age of eighteen, in addition to the Members themselves and senior congressional staff. Much has changed since the Ban Conflicted Trading Act was first introduced in 2018. It's now clear that Members' spouses and dependents should be covered by these reforms. In addition, there is a political will in Congress and among the American public to do so.

The amended text would also tighten requirements for qualified blind trusts, ensuring that the trustee does not have a close relationship with the grantor—be it Members, their spouse, or congressional staff—and requiring the trustee to certify annually that they have not provided knowledge of the trust's workings to the grantor. The trustee is further required to divest all securities initially placed in the trust, thereby ensuring the grantor has no knowledge of what investments are held in the trust and avoiding any potential conflicts of interest based on knowledge of the initial holdings placed in the trust.

The penalties for violating the Ban Conflicted Trading Act have also been overhauled, adding minimum fines for each day the violations continue. For example, in the event that a Member has made a prohibited purchase of an individual security and continues to reap the benefit of that investment, a one-time penalty is not sufficient to

[1] See the amended text and section-by-section attached below.

deter this violation; instead, under the amended text, the Member would be fined $500 per day until the purchased investment is divested.

Numerous additional changes have been made to clarify certain provisions or address special situations, including clarifying the definition of a widely held investment fund, addressing the treatment of certain investment vehicles, like 529 education savings plans, and specifying the treatment of gifted or inherited investments, among other things.

Madam Chairwoman, we have never been closer to enacting such meaningful reform of Member stock trading regulations. We look forward to the hearing on April 7, and we ask that, following this hearing, the Committee move without delay to mark up the Ban Conflicted Trading Act with the attached changes.

We welcome the Committee's feedback on these proposed changes to H.R. 1579, and we look forward to working with you to pass these important reforms this Congress.

Sincerely,

Raja Krishnamoorthi Member of Congress	Alexandria Ocasio-Cortez Member of Congress	Joe Neguse Member of Congress

An Amendment to HR 1579, the Ban Conflicted Trading Act

Section-by-Section of Proposed Changes

Section 2. Definitions

- Expands and clarifies what investments covered persons can buy and sell.
    - Clarifies that covered investments cannot be bought or sold through an investment vehicle that the covered person controls, including
        - 529 education savings accounts;
        - employee benefit plans;
        - deferred compensation plans;
        - retirement accounts;
        - trusts; and
        - other such investment vehicles
    - Clarifies the definition of "widely held investment fund," based on House Ethics Committee financial disclosure guidance.
        - 2(C)i: a widely held investment fund, such as a mutual fund or exchange-traded fund–
            - (I) which the covered person does not exercise control over directly or indirectly;
            - (II) the financial interests of which, the covered person does not have the ability to exercise control over, directly or indirectly;
            - (III) the manager of which, with whom the covered person does not have a close personal or business relationship;
            - (IV) the assets of which are widely diversified, not being concentrated in any industry, business, single country other than the United States, or bonds of a single State.
    - Adds a line explicitly allowing investments in Federal, State, or local government employee retirement plans.
- Clarifies the definition of a Member of Congress, using existing Ethics in Government Act definition.
- Adds spouses and dependents under 18 to covered persons.

Section 3. Prohibitions

- Clarifies that covered persons may not receive covered investments as a gift (this does not preclude inherited investments).

Section 4. Requirements (this Section was previously titled Exceptions)

- Clarifies the rules governing covered investments already owned by covered persons prior to enactment of this bill.
    - Clarifies that dividends from these investments cannot be reinvested.
    - Clarifies that these investments cannot be bought or sold at the direction of anyone outside of a blind trust.
        - The existing language could potentially be misconstrued to allow others to buy or sell these investments at the behest of the covered person.
    - Adds new exceptions allowing inherited investments and investments received as primary compensation to be treated as investments already owned by covered persons. (i.e. they can be held, but not bought or sold except through a blind trust or divestiture)
- Adds an effective date of Jan 1, 2027 for spouses and dependents (the effective date for Members and staff is the date of enactment of the bill).

Section 5. Trusts

- Adds a provision requiring Ethics to issue guidance on requirements for qualified blind trusts.
- Stipulates additional requirements for qualified blind trusts–

- The trustee must divest of all initial securities placed in the trust within 6 months of establishing the trust (and buy other securities instead);
- The trustee must certify annually that the trustee has not provided knowledge of the trust's assets or the trust's transactions to the grantor; and
- The trustee may not have a close personal or business relationship with the covered person.

Section 6. Administration and Enforcement

- Adds a provision prohibiting the Ethics Committees from extending deadlines specified in the bill.
- Clarifies the penalties and adds additional penalties for different violations.
  - In the case of a sold investment, the penalty is 10% of the value of such investment at the time of sale.
  - In the case of a purchased investment, the penalty is at least $500 per day that the covered person is in violation, until they divest the purchased investment.
  - In the case of a net short position, the penalty is at least $500 per day until the covered person is no longer in a net short position in any security.
  - In the case of a covered person serving as an officer or member of a for-profit corporation, the penalty is at least $500 per day until the covered person steps down from such positions.

....

(Original Signature of Member)

117TH CONGRESS
2D SESSION

H. R. ____

To prohibit Members of Congress from purchasing or selling certain investments, and for other purposes.

IN THE HOUSE OF REPRESENTATIVES

Mr. KRISHNAMOORTHI introduced the following bill; which was referred to the Committee on ______________________________

A BILL

To prohibit Members of Congress from purchasing or selling certain investments, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Ban Conflicted Trading Act".

SEC. 2. DEFINITIONS.

In this Act—

(1) the term "commodity" has the meaning given the term in section 1a of the Commodity Exchange Act (7 U.S.C. 1a);

(2) the term "covered investment"—

(A) means investment in a security, a commodity, or a future, or any comparable economic interest acquired through synthetic means such as the use of a derivative;

(B) includes any investment described in subparagraph (A), which is bought or sold through an investment vehicle that the covered person controls, including—

(i) qualified tuition programs described in section 529 of title 26, United States Code, or in a Coverdell education savings account under section 530 of that title;

(ii) employee benefit plans;

(iii) deferred compensation plans;

(iv) retirement accounts;

(v) trusts; and

(vi) other such investment vehicles; and

(C) does not include—

(i) a widely held investment fund, such as a mutual fund or exchange-traded fund—

(I) which the covered person does not exercise control over directly or indirectly;

(II) the financial interests of which, the covered person does not have the ability to exercise control over, directly or indirectly;

(III) the manager of which, with whom the covered person does not have a close personal or business relationship; and

(IV) the assets of which are widely diversified, not being concentrated in any industry, business, single country other than the United States, or bonds of a single State;

(ii) any investment fund held in a Federal, State, or local government employee retirement plan;

(3) the term "covered person" means—

(A) a Member of Congress as defined in section 109(12) of the Ethics in Government Act of 1978 (5 U.S.C. App. 109(12));

(B) a spouse of a United States Senator, Representative in Congress, Delegate to Congress, or the Resident Commissioner from Puerto Rico;

(C) a dependent, who is under the age of 18, of a United States Senator, Representative in Congress, Delegate to Congress, or the Resident Commissioner from Puerto Rico; and

(D) an officer or employee of Congress as defined under section 109(13) of the Ethics in Government Act of 1978 (5 U.S.C. App. 109(13));

(4) the term "future" means a financial contract obligating the buyer to purchase an asset or the seller to sell an asset, such as a physical commodity or a financial instrument, at a predetermined future date and price;

(5) the term "security" has the meaning given the term in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)); and

(6) the term "Select Committee on Ethics" means the Select Committee on Ethics of the Senate

or the Committee on Ethics of the House of Representatives.

SEC. 3. PROHIBITIONS.

(a) TRANSACTIONS.—Except as provided in sections 4 and 5, no covered person may—

(1) purchase or sell any covered investment;

(2) enter into a transaction that creates a net short position in any security; or

(3) receive a covered investment by gift.

(b) POSITIONS.—A covered person may not serve as an officer or member of any board of any for-profit association, corporation, or other entity.

SEC. 4. REQUIREMENTS.

(a) INVESTMENTS HELD BEFORE TAKING OFFICE.—

(1) IN GENERAL.—Except as provided in paragraph (3), a covered person may have control over or knowledge of the management of any covered investment owned by the covered person—

(A) as of the day before the date on which the covered person took office; or

(B) received during office in accordance with subsection (c).

(2) PROHIBITION ON PURCHASING OR SELLING.—Investments described in paragraph (1) may

not be bought or sold, including through the reinvestment of dividends, by any person except in the case of—

(A) converting the investment into a qualified blind trust described in section 5; or

(B) divesting of any investment in accordance with subsection (b).

(b) DIVESTITURE.—A covered person may sell a covered investment during the 6-month period beginning on—

(1) the date on which the covered person takes office or begins employment, as applicable;

(2) the date of enactment of this Act;

(3) the date on which the covered person inherits a covered investment; or

(4) the date on which a covered person receives covered investments as compensation from their primary occupation.

(c) INVESTMENTS RECEIVED DURING OFFICE.—

(1) INHERITED INVESTMENTS.—In the event that a covered person receives a covered investment through bequest or other forms of inheritance, the such investment is subject to the requirements under subsection (a).

(2) PRIMARY COMPENSATION.—In the event that a covered person receives covered investments as compensation from their primary occupation, such investments are subject to the requirements under subsection (a).

(d) EFFECTIVE DATE.—This Act shall apply to individuals described in subparagraphs (B) and (C) of section 2(3) beginning on January 1, 2027.

SEC. 5. TRUSTS.

(a) IN GENERAL.—On a case-by-case basis, the Select Committee on Ethics may authorize a covered person to place their covered investment in a qualified blind trust approved by the committee under section 102(f) of the Ethics in Government Act of 1978 (5 U.S.C. App. 102(f)).

(b) BLIND TRUST.—

(1) CRITERIA.—A blind trust permitted under this section shall meet the criteria in section 102(f)(4)(B) of the Ethics in Government Act of 1978 (5 U.S.C. App. 102(f)(4)(B)), unless an alternative arrangement is approved by the Select Committee on Ethics.

(2) REQUIREMENTS FOR TRUSTEES.—With respect to a trust under this Act, the trustee—

(A) shall divest of all initial securities placed in the trust within 6 months of establishing the trust;

(B) shall certify annually that the trustee has not provided knowledge of the trust's assets or the trust's transactions to the grantor; and

(C) may not have a close personal or business relationship with the covered person.

(3) GUIDANCE.—In carrying out this section, the Select Committee on Ethics shall issue guidance on the requirements relating to qualified blind trusts such that the guidance issued applies equally to each covered person described in section 2(3).

SEC. 6. ADMINISTRATION AND ENFORCEMENT.

(a) ADMINISTRATION.—

(1) IN GENERAL.—The provisions of this Act shall be administered by the Select Committee on Ethics.

(2) GUIDANCE.—The Select Committee on Ethics are authorized to issue guidance on any matter contained in this Act.

(b) ENFORCEMENT.—Whoever knowingly fails to comply with this Act shall be subject to a civil penalty of—

(1) with respect to the sale of a covered investment, 10 percent of the value of such investment at the time of sale;

(2) with respect to the purchase of a covered investment, an amount, that may exceed $500, for each day during the period beginning on which the covered person is determined to be in violation and ending on the date the covered person is determined to be in compliance;

(3) with respect to a violation of section 3(a)(2), an amount, that may exceed $500, for each day during the period beginning on which the covered person is determined to be in violation and ending on the date the covered person is determined to be in compliance; and

(4) with respect to a violation of section 3(b), an amount, that may exceed $500, for each day during the period beginning on which the covered person is determined to be in violation and ending on the date the covered person is determined to be in compliance.

(c) RULES OF CONSTRUCTION.—Nothing in this Act may be construed to grant the Select Committee on Ethics the authority to extend any deadlines in this Act.

THE WALL STREET JOURNAL.

HIDDEN INTERESTS

Dozens of Federal Judges Had Financial Conflicts: What You Need to Know

A Wall Street Journal investigation finds more than 130 federal judges unlawfully ruled in cases involving companies in which they or their families held shares

By Michael Siconolfi, Coulter Jones Follow *, Joe Palazzolo* Follow *and James V. Grimaldi* Follow
Updated Mar. 17, 2022 10:46 am ET

SHARE TEXT

Listen to article (11 minutes)

A Wall Street Journal investigation found that federal judges around the nation have violated U.S. law and judicial ethics by overseeing 1,006 court cases involving companies in which they or their family owned stock.

As a result of the Journal's reporting, judges in 836 cases have notified courts that they presided in the lawsuits improperly and that the cases are eligible to be reopened.

How many judges broke the law?

In the most expansive investigation of judicial stockholdings in the U.S., the Journal in September 2021 revealed that 131 federal judges improperly heard 685 court cases between 2010 and 2018 in which they or their family members owned shares of companies that were plaintiffs or defendants in the litigation. Two of the judges sat on appellate courts; the other 129 were district judges, also called trial judges. Since its initial review, which examined civil cases, the Journal found additional judges and more violations.

About two-thirds of federal district judges disclosed holdings of individual stocks, and nearly one of every five of those who did improperly heard at least one case involving a company in which they or their families owned a stake.

RELATED LINKS

- 131 Federal Judges Broke the Law by Hearing Cases Where They Had a Financial Interest
- Federal Judges or Their Brokers Traded Stocks of Litigants During Cases
- Judges Held Off Congress's Efforts to Impose Ethics Rules—Until Now

What is the law?

Nothing bars judges from owning stocks, but a 1974 federal law prohibits any "ownership of a legal or equitable interest, however small," in a party to a case before a judge. That law and the Judicial Conference of the U.S., the federal courts' policy-making body, require judges to avoid even the appearance of a conflict.

The ban on holding even a single share of a company while presiding in a case involving the firm means judges must be vigilant about their assets, including informing themselves about stockholdings of spouses and minor children.

The Judicial Conference requires courts to use conflict-checking computer software to help identify cases where judges should bow out. Judges needn't disqualify themselves from cases involving banks where they have mortgages or checking or savings accounts, nor do they need to recuse because of any mutual-fund holdings.

How pervasive is the problem?

The Journal found judges failing to disqualify themselves as required in every region of the country. They included judges appointed by nearly every president from Lyndon Johnson to Donald Trump.

When there were contested motions in cases involving companies the judges had a financial stake in, two out of three of their rulings on the motions were in favor of those companies.

Dozens of judges or their families not only owned shares in companies in their courtrooms but reported that they or their brokers traded the shares while the judges were presiding in the cases.

Legal experts said the activity the Journal found amounts to a pervasive disregard for the judicial conflict-of-interest laws. Indiana University Law Professor Charles Geyh said that, in isolation, a violation could be viewed as an oversight. But the Journal's overall findings raise "a more systemic problem of judges chronically neglecting their duty to disqualify in such cases."

How did WSJ do it?

The Journal reviewed hundreds of financial disclosure forms filed annually from 2010 to 2018 with the Administrative Office of the U.S. Courts. The forms, filed by federal trial and appellate judges, aren't online. The Journal used the courts' data as obtained and digitized by the Free Law Project, a nonpartisan legal-research nonprofit.

Then the Journal compared judges' stockholdings to tens of thousands of court dockets, finding 685 violations. Scholars who reviewed the Journal's analysis said its methodology was sound. The Journal later gained access to some 2019 financial disclosures, and identified more than 300 additional judicial violations, including in some older cases. The rest of the 2019 forms are expected to be released this year.

The Free Law Project has posted its database of more than 250,000 pages of judges' financial disclosures drawn from over 26,000 electronic files. The group requested the files from the federal judiciary beginning in 2017 and has been gathering them since then.

What have judges said?

Judges offered a variety of explanations for the violations. Some blamed court clerks. Some said their lists of companies to avoid had misspellings that foiled the conflict-screening software. Some said they had only nominal roles in the cases, such as confirming settlements, though there is no legal exemption for such roles.

Some judges misunderstood the law, saying erroneously that they didn't have to recuse themselves because their stock was held in accounts run by professional money managers.

One judge who had 36 recusal violations, after initially saying he "never really paid much attention" to his stockholdings and wasn't familiar with the ethics law, told the Journal: "I am embarrassed that I did not properly understand and apply the stock ownership rule."

Some judges since have sold shares in family accounts. After the Journal contacted U.S. District Judge Liam O'Grady about a financial conflict involving an Amazon.com Inc. case he had been hearing for 20 months, his wife's investment adviser in December sold the Amazon shares. One of the defendants in the case has asked that a new judge be appointed to rehear the case.

The Administrative Office of the U.S. Courts in October warned judges in a memo they are required to keep informed about their finances and maintain timely lists of parties that are off limits. Judge Roslynn Mauskopf, director of the office, wrote that judges may not rely on accounts managed by financial advisers to avoid their recusal obligations. "Up-to-date recusal lists are the most effective tool for conflict screening," she wrote.

The Potter Stewart U.S. Courthouse in Cincinnati.
PHOTO: SAM GREENE/THE CINCINNATI ENQUIRER/ASSOCIATED PRESS

Some district courts have gone further to urge judges to be more vigilant. In a Dec. 21 memo, the U.S. District Courts of the Ninth Circuit, in California, wrote that "in light of the importance of conflict screening, I am writing to urge you to compare, as expeditiously as possible, your 2019 and 2020 financial disclosure reports against all cases that were assigned to you during the periods covered by these reports." A similar memo and a best-practices tipsheet were sent out in November to judges in the Fifth Circuit.

What has been the fallout?

After being alerted to violations by the Journal, judges have directed court clerks as of March 17, 2022, to notify parties in 836 lawsuits that they should have disqualified themselves and that cases could be reassigned and reopened.

In one instance, Rodney Gilstrap, one of America's most prominent federal judges, acknowledged in court notices that he may have violated the law in 138 lawsuits identified by the Journal between 2011 and 2018 by hearing cases that involved companies in which he or his wife had a financial interest.

A new judge was assigned to an asbestos case in South Carolina in December after the widow of a deceased veteran objected to the previous judge's ownership of investments in some of the defendant companies. In two other recusal violations, the appearance of a conflict for the judges has become enmeshed with arguments on appeal in circuit courts in New York and California.

In another case, in an Alabama federal court, a judge ruled against two homeowners in a foreclosure case against Wells Fargo & Co. The judge had bought Wells Fargo stock about two weeks after receiving the case. "This is outrageous," one of the homeowners said when told the judge held the bank shares. "How am I supposed to know she owns stock in Wells Fargo?"

The homeowners asked the court to reopen the case. The court has assigned a new judge to their suit. The court clerk said the judge's stockholding didn't affect her decisions in the case.

Has there been any government response?

In direct response to the Journal articles, the House held a hearing and in December passed a bill to streamline and expedite public access to judges' financial-disclosure forms, which now are infrequently made public. Senate sponsors of a similar bill are seeking to pass it in 2022, a congressional aide said. Judiciary Committee members have introduced several other bills to modernize the judiciary's ethics, disclosure and transparency rules, which could be swept into omnibus legislation.

The U.S. Senate unanimously passed legislation in February to require Supreme Court justices and federal judges to promptly post online their stock trades and financial holdings

The federal judiciary has been fighting back on the legislation, but lawmakers in both parties are steadfast in pushing it through.

"The need for change is glaring," said Rep. Hank Johnson, a Georgia Democrat who heads the House Judiciary Committee's courts subcommittee, "especially when you get the kinds of reports that The Wall Street Journal led where you see that the law is being abused by members of the judicial branch, not just by a few, but dozens after dozens of federal district court judges."

In an October letter to Chief Justice John Roberts, who heads the judiciary, Sen. Elizabeth Warren (D., Mass.) and Rep. Pramila Jayapal (D., Wash.) asked for information related to the Journal's "Hidden Interests" series. They said they were proposing legislation that would impose civil sanctions for recusal violations and a ban on judges "owning individual stocks, radically reducing the likelihood of conflicts of interest without the need for recusal proceedings."

Citing the Journal coverage, Chief Justice Roberts pledged in December to improve the federal judiciary's ethics training and compliance. "Let me be crystal clear: the Judiciary takes this matter seriously. We expect judges to adhere to the highest standards, and those judges violated an ethics rule," the chief justice said in his year-end report.

What can you do in your case?

If a judge notifies a court clerk of a recusal violation, parties have the option to ask the court to rehear the case with a different judge.

If you have a pending case involving a company, you can ask your lawyer to contact the Administrative Office of the U.S. Courts for the latest financial disclosure forms of the judge to determine whether he or she has any conflicts or violations. But disclosures are filed only annually.

If anyone requests to see judges' financial disclosures, the judges are told who asked. Some lawyers say this creates a disincentive for them to ask, out of concern about annoying judges in whose courtrooms they frequently appear.

Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

The Challenges Of Prosecuting Congressional Insider Trading

By **Robert K. Kelner, Peter Koski and Clayton Bailey** (June 18, 2020, 5:32 PM EDT)


Robert K. Kelner


Peter Koski


Clayton Bailey

Allegations that U.S. senators traded on confidential briefings about COVID-19 have brought new enforcement attention to the rarely used Stop Trading on Congressional Knowledge, or STOCK, Act.

In a sign of significant escalation, last month the FBI reportedly seized the mobile phone of Sen. Richard Burr, R-N.C., in connection with one such investigation, even as the U.S. Department of Justice announced it was closing investigations into Sens. Kelly Loeffler, R-Ga., Jim Inhofe, R-Okla., and Diane Feinstein, D-Calif.

The FBI also reportedly served a warrant on Apple Inc. seeking data stored in Burr's iCloud account.

The STOCK Act, first enacted in 2012, prohibits members of Congress and other government officials from trading on material nonpublic information "derived from such person's position as a Member of Congress or employee of Congress or gained from the performance of such person's official responsibilities."[1]

While these allegations may resemble traditional insider trading, the challenges for prosecutors are unique and exacting. Charges under the STOCK Act have never been brought against a member of the legislative branch, and prosecutors face at least two potentially existential challenges due to the nature of legislative work.

First, the U.S. Constitution's speech or debate clause may prevent the DOJ from satisfying an essential element of the offense — proving what legislators learned in the course of their official duties.

Second, the Confidential Information Procedures Act, or CIPA, may force prosecutors to risk publicizing classified information as a consequence of bringing an enforcement action.

The Speech or Debate Clause

In order to prove a violation of the STOCK Act, prosecutors must prove that the nonpublic information acted on by a member of Congress was "derived from such person's position" or "gained from the performance of such person's official responsibilities." But for legislators, much of the information learned in the course of their official responsibilities could be shielded by the immunity granted under the speech or debate clause.

The clause presents a challenge not present in the insider trading case brought against former Rep. Chris Collins, R-N.Y., who was convicted of trading on material nonpublic information he obtained while serving on the board of a publicly traded company, as opposed to nonpublic information learned through his legislative activities.

Prosecutors could therefore be categorically barred from presenting the evidence necessary even to secure an indictment. Notably, in a prior civil STOCK Act investigation into whether a congressional staffer provided material nonpublic information to a lobbyist, the U.S. Securities and Exchange Commission was forced to abandon significant parts of its subpoena to the staffer and the House Ways and Means Committee because of the speech or debate clause.[2]

The Constitution provides that "for any Speech or Debate in either House, [senators and representatives] shall not be questioned in any other Place."[3] The clause was:

> designed to assure a co-equal branch of the government wide freedom of speech, debate, and deliberation without intimidation or threats from the Executive Branch. It thus protects members against prosecutions that directly impinge upon or threaten the legislative process.[4]

Members of Congress and their staff are thus "immune from liability for their actions within the legislative sphere."[5]

Of practical importance, the U.S. Court of Appeals for the D.C. Circuit has held that the clause creates a broad nondisclosure privilege that protects against the disclosure of legislative material.[6] In other words, not only are members of congress immune from prosecution for legislative acts, but — at least within the D.C. Circuit — they also cannot be compelled to produce documents related to actions within the legislative sphere.

Here, application of the speech or debate clause requires a careful, fact-driven analysis of how the member of Congress learned the nonpublic information in question. It may be possible that some STOCK Act prosecutions can be pursued without running afoul of the clause.

But, like here, if the allegation is that a senator or representative learned the information during a formal committee briefing, the clause would likely preclude the introduction of evidence, or even the allegation in an indictment, of the information provided during that briefing, thereby precluding the prosecution from proving an essential element of the offense. The U.S. Supreme Court has held that the clause applies to committee hearings,[7] and courts would likely extend that application to official committee briefings.[8]

The FBI's seizure of Burr's cell phone, and its collection of Burr's iCloud data, presents an interesting wrinkle regarding the speech or debate clause. First, the clause is likely to complicate the FBI's review of Burr's communications. Information received in the course of legislative activity is likely to be on Burr's phone, and should be protected from review, at least within the D.C. Circuit. Second, the seizure may indicate a creative attempt by investigators to overcome the obstacles presented by the speech or debate clause.

Reports have indicated that Burr and his brother-in-law dumped their stock on the same day. Communications sent from Burr to individuals outside the legislative branch are likely fair game for investigators, as the Supreme Court has ruled that the dissemination of information outside the legislative branch is unprotected by the speech or debate clause.[9]

This principle even includes official communications, like press releases, that describe legislative acts, such as a vote or sponsorship of a bill.[10] Any communications by Burr with his brother-in-law, even to share information that he learned through the course of his legislative duties, would therefore likely be unprotected by the speech or debate clause.

On this point, it is worth noting that in the SEC's investigation described above, the district court ruled that a congressional staffer's communications to a lobbyist are categorically unprotected by the speech or debate clause, declaring that documents relating to such communications must be produced to the SEC.[11]

The government may also believe that the phone could provide evidence of secondary charges, such as charges related to a failure to preserve potentially incriminating emails or text messages. This type of charge — and the evidence necessary to prove it — is unlikely to be burdened by the same constitutional challenges associated with enforcing the STOCK Act.

The Confidential Information Procedures Act

If prosecutors manage to collect the evidence necessary to bring a STOCK Act case to trial, they face another problem: The potential disclosure of classified information. Because a STOCK Act prosecution requires evidence that a member of Congress received specific nonpublic information in the course of official duties, there is a risk that the information itself, or the source of that information, is classified.

A member of Congress charged with violating the STOCK Act may also seek to put that information in context by presenting other information learned in the course of those duties, even if that information remains classified. For someone like Burr, who until very recently served as chair of the Senate Intelligence Committee, that defense seems even more probable.

Given his position, the classified information may be significant, and release at trial may prove harmful to the national interest. This type of defense strategy, referred to as graymailing, has frustrated the government's ability to fully pursue its law enforcement interests in several recent high-profile cases.

CIPA is a procedural law that seeks to balance a defendant's right to a fair trial with the government's interest in protecting classified information. CIPA requires defendants to provide the prosecution with notice of their intent to put on classified information as evidence at trial, and requires the court to hold a pretrial hearing for the purpose of making admissibility rulings before a jury is even empaneled.[12]

Should the court rule that classified information is admissible, the government may move for substitution of an unclassified summary of the information at issue that "will provide the defendant with substantially the same ability to make his defense as would disclosure of the classified information."[13]

Should the government lose such a motion, it will be forced to weigh the importance of its prosecution against the importance of preventing the public disclosure of the classified information. That balance will depend on the individual circumstances of the case, but it is not a situation that any prosecutor welcomes.

Robert K. Kelner is a partner and chair of the election and political law practice group at Covington & Burling LLP.

Peter Koski is of counsel at the firm. He previously served as deputy chief of the DOJ's Public Integrity Section.

Clayton Bailey is an associate at Covington.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] 15 U.S.C. § 78u-1(g)(1).

[2] Sec. & Exch. Comm'n v. Comm. on Ways & Means of the U.S. House of Representatives, 161 F. Supp. 3d 199, 246 (S.D.N.Y. 2015).

[3] Art. I, Sec. 6, Cl. 1.

[4] Gravel v. United States, 408 U.S. 606, 616 (1972).

[5] Doe v. McMillan, 412 U.S. 306, 312 (1973).

[6] United States v. Rayburn House Office Building, 497 F.3d 654, 655, 660 (D.C. Cir. 2007).

[7] United States v. Brewster, 408 U.S. 501, 509, 512 (1972).

[8] Gravel, 408 U.S. at 624 (holding that the Clause applies broadly to Members' conduct within the "sphere of legitimate legislative activity").

[9] Hutchison v. Proxmire, 443 U.S. 111, 133 (1979); Brewster, 408 U.S. at 512.

[10] Hutchison, 443 U.S. at 133.

[11] Sec. & Exch. Comm'n, 161 F. Supp. 3d at 245-46.

[12] 18a U.S.C. §§ 4, 6.

[13] 18a U.S.C. § 6(c)(1)(B).

59 members of Congress have violated a law designed to stop insider trading and prevent conflicts-of-interest

Dave Levinthal   Updated

Marianne Ayala/Insider

Insider and other media have identified numerous US lawmakers not complying with the federal STOCK Act.
Their excuses range from oversights, to clerical errors, to inattentive accountants.
Ethics watchdogs — and even some in Congress — want to ban lawmakers from trading individual stocks.
See more stories on Insider's business page.

Insider and several other news organizations have identified 59 members of Congress who've recently failed to properly report their financial trades as mandated by the Stop Trading on Congressional Knowledge Act of 2012, also known as the STOCK Act.

Congress passed the law a decade ago to combat insider trading and conflicts of interest among their own members and force lawmakers to be more transparent about their personal financial dealings. A key provision of the law mandates that lawmakers publicly — and quickly — disclose any stock trade made by themselves, a spouse, or a dependent child.

But many members of Congress have not fully complied with the law. They offer excuses including ignorance of the law, clerical errors, and mistakes by an accountant. Insider has chronicled this widespread nature of this phenomenon in a new project, "**Conflicted Congress**."

While lawmakers who violate the STOCK Act face a fine, the **penalty is usually small** — $200 is the standard amount — or waived by House or Senate ethics officials. Ethics watchdogs and even some members of Congress have called for stricter penalties or **even a ban** on federal lawmakers from trading individual stocks. On Capitol Hill, lawmakers are **now seriously debating** such a ban.

Here are the lawmakers discovered to have recently violated the STOCK Act — to one extent or another:

Banning Lawmakers From Trading Stocks Won't Fix Congress

But it will make the market worse.

Jennifer Schulp 2.22.2022 4:10 PM

|

(Illustration: Lex Villena; Indiloo, Dragonimages)

After a collection of questionable stock trades by members of Congress at the beginning of the pandemic, and similar trading scandals in the federal judiciary and the Federal

Reserve, there is growing momentum to ban members of Congress from trading or even holding individual stocks while in office. Recent polls show wide support from the American public to impose limits on holding individual stocks, and both Republicans and Democrats have introduced bills with different frameworks for limiting lawmakers' financial holdings. Even House Speaker Nancy Pelosi (D–Calif.)—who has historically opposed such a bill—has recently signaled her willingness to advance such legislation.

A leading argument in favor of banning congressional stock ownership is that such a ban is needed to prevent legislators from insider trading. This is wrong because restricting Congressional trading not only has the potential to harm markets, but a focus on insider trading obscures the broader question of how to address lawmakers who may use their positions for personal, financial gain.

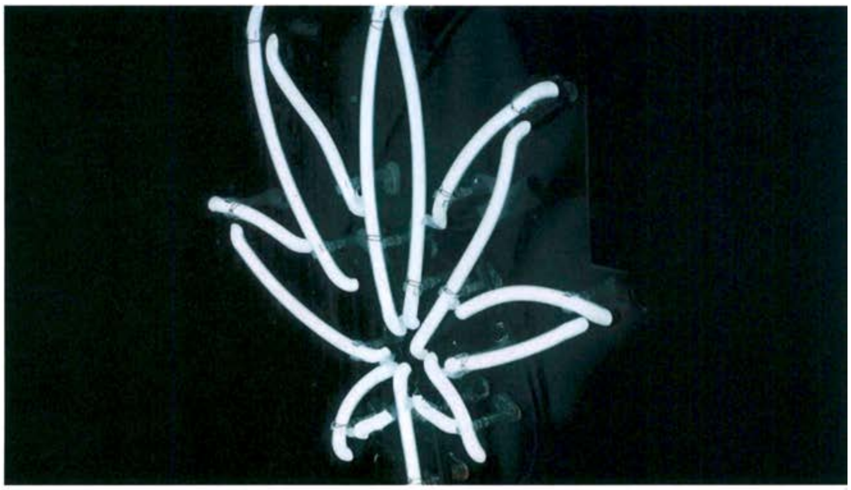
Illegal insider trading is when someone trades a stock misusing non-public information that impacts the stock's value. The STOCK Act, passed in 2012, made clear that trading on non-public information derived from a member of Congress's official position is an insider trading violation. The Securities and Exchange Commission considers insider trading to "undermine investor confidence in the fairness and integrity of the securities markets."

Those who support limits on congressional investments point to well-timed trades and research showing that members of Congress outperform normal people in the stock market. That research tends to draw on trading data from before the STOCK Act, and some studies, including this recent one by the National Bureau of Economic Research, have found no particular outsized returns for lawmakers. Although voters look poorly on elected representatives who may be making unfair gains, it's a leap to conclude from the body of research that unlawful insider trading is widespread on Capitol Hill.

Prohibitions on insider trading already harm market efficiency by preventing a stock's price from reflecting all of the information known about the stock. A broad-based ban on stock trading or ownership would add to that market inefficiency by preventing lawmakers from contributing information that allows the markets to engage in price discovery. Because the type of information that members of Congress are privy to relates not just to individual companies, but to entire industries and the whole economy, such information should actually be absorbed quickly into the market—particularly when doing so does not violate existing insider trading law—rather than kept out.

The fact that prosecuting insider trading violations by members of Congress is challenging, and lawmakers from both parties have a poor record in complying with trade reporting requirements, does not mean that a prophylactic ban on holding individual stocks is a good idea or a necessary one.

Top Articles

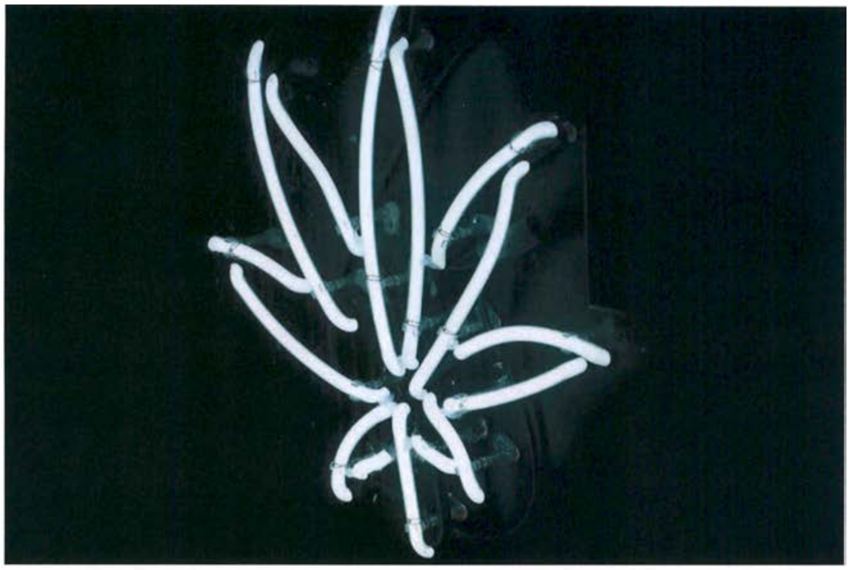


Read More


STUDENT LOAN


FAKE
NEWS

D.C. City Council Narrowly Fails To Destroy theCountry's Freest Marijuana Market



Justifying a stock-ownership ban based on insider trading rules also makes little sense. The issue is not with maintaining investor confidence in the market—the stated reason for insider trading rules. The issue is with maintaining voter confidence in their elected officials—two very different issues. The more apt question when considering limitations on congressional financial holdings is whether, and to what degree, members of Congress should be permitted to gain personal financial advantage from their positions.

The question, properly framed, focuses on potential conflicts of interest faced by members of Congress. Uniquely positioned members of Congress have information that may impact the value of particular stocks while also having the ability to impact the value of particular stock by legislating, by calling for investigations, or by otherwise exerting their political influence.

That means potential conflicts of interest can exist not only in a member's individual stock ownership, but also in fund investments, crypto holdings, or business interests of lawmakers, their families, or their staff. Managing these potential conflicts of interest is a complex task, asking lawmakers and voters alike to determine the proper balance between lawmakers' personal financial interests, their stake in particular issues, and their ability to represent their constituents. At best, focusing only on stock ownership and trading provides an incomplete picture.

Insider trading law has a reputation for lacking clarity and generating confusion. It would be a mistake to add to that confusion by attempting to justify a ban on congressional stock ownership in the name of preventing illegal insider trading, particularly when the motivation for such restrictions is protecting Congress's integrity, not the market's. Instead, potential solutions should be evaluated against the full range of financial conflicts of interest that members of Congress face.

Republican Rep. Rodney Davis doesn't trade stocks. But that doesn't mean he's ready to stop other members of Congress who do.

Kimberly Leonard Apr 5, 2022, 10:34 AM

Rep. Rodney Davis of Illinois is the top Republican on the Committee on House Administration. The committee is holding a hearing about congressional stock trading.
Alex Wong/Getty Images

Davis is the top Republican for the Committee on House Administration.
The panel is scheduled to meet April 7 to debate banning lawmakers from trading stocks.
Davis left the door open to a ban but stressed the House must have better ethics training.

Republican Rep. Rodney Davis — who's about to have a lot of influence over members of Congress' personal finances — said he's loath to force his colleagues to stop trading stocks.

Davis, of Illinois, is the ranking Republican on the Committee on House Administration, which on Thursday will conduct a congressional hearing that will include discussions about whether Congress should ban lawmakers from buying and selling individual stocks.

"I don't want to pigeonhole myself into laying out what I think my priorities are," Davis said when asked in a recent interview whether he could support a stock trading ban.

He left a lot of room for where he'd eventually land, though, describing himself as being in the "discovery mode" on the issue and throwing out a few ideas for how to improve rules around stock trading.

One option would be to make data about members' personal finances far more accessible to the public, he said.

Under current law, the 2012 Stop Trading on Congressional Knowledge Act, or STOCK Act, members have few limits on stock trading but they have to quickly and publicly report all of their trades.

For Davis, it's that reporting requirement alone that's enough to make the five-term congressman voluntarily abstain from actively trading stocks. This way, he only has to report his finances annually, not weekly or monthly.

"It is a pain in the butt to fill out the financial disclosures if you have new investments on a regular basis," Davis said. "That type of reporting deters a lot of members like me from wanting to participate."

But that also means, Davis said, that he might not have the full picture on the issue until he hears from colleagues that do choose to actively trade stocks.

More than one in 10 members of Congress has violated the STOCK Act by failing to report stock trades on deadline, according to Insider's "Conflicted Congress" investigation, published in December.

"Conflicted Congress" also found numerous examples of conflicts of interest, including that four members of Congress or their spouses have either currently or recently invested money in Russian companies at a time when Russia has invaded Ukraine.

These are big reasons why there's a renewed push to make changes to the law.

Davis speaks at a news conference next to Minority Leader Kevin McCarthy of California.
Kevin Dietsch/Getty Images

'Playground for the wealthy'?

I asked Davis what he thought about two House bills that would ban lawmakers from trading individual stocks and have them place existing holdings into a blind trust.

The blind trust arrangement would require lawmakers to cede control of their personal investments to an independent trustee. As designed, members of Congress wouldn't know what the trustees bought or sold in their name until weeks or months after the fact.

While at least 10 members of Congress have already established congressionally approved qualified blind trusts, it can be expensive and time-consuming to formalize. The process would be a significant undertaking particularly for a first-time politician running for the US House, a position that is up for re-election every two years.

Davis said he wants to dive into the specifics of what members would have to do to get a blind trust, including what price tag they'd face.

"I do not want the House of Representatives to only become a playground for the wealthy since many of the discussion points being thrown around include some costly provisions that could price out future members of Congress," he said.

If Davis decides to formally oppose a stock trading ban, it could put him at odds with the chamber's top Republican.

Minority Leader Kevin McCarthy of California is poised to become House speaker if Republicans win back the House in November, and he reportedly wanted to make promises of STOCK Act reforms a big part of the GOP platform for the midterm elections.

Davis said he hasn't talked to McCarthy directly about the matter, adding, "It doesn't mean we won't be on the same page when this hearing comes up, because we certainly will be."

House Speaker Nancy Pelosi speaks with Democratic Rep. Zoe Lofgren, who is chairwoman of the Committee on House Administration.

Chip Somodevilla/Getty Images

True bipartisanship? It's TBD.

It's not clear how bipartisan an eventual STOCK Act reform effort will be.

Republicans and Democrats on the committee told me two versions of what happened leading up to the planning of

Thursday's hearing.

Republicans insisted that they asked Democrats whether they could have members of Congress speak on panel about their experiences trading stocks, and what it was like to report their finances.

Democrats deny that Republicans ever asked.

Davis also told me that he'd been cut out of a lot of the preparation for the hearing. House Speaker Nancy Pelosi directed Committee on House Administration Chairwoman Zoe Lofgren to look at STOCK Act compliance and to consider harsher penalties for those who violate the law.

Lofgren's spokesman, Peter Whippy, said that Thursday's hearing is part of that process.

Davis said he was glad the hearing would be happening and that he hoped both parties could hammer out solutions together.

He stressed that the STOCK Act's accomplishments shouldn't be underestimated. The public has enhanced access to details about politicians' financial trades thanks to the law's requirements, he said.

Meanwhile, if members face questions from the media or elsewhere about potential conflicts of interests in the trades they make, then they should be ready to answer them, he said.

Still, Davis has considered some reforms, such as improving new-member orientation so that congressional ethics and disclosure rules are clearer. He said he was particularly concerned about freshmen members of Congress who appeared to have trouble following the rules.

Two notable examples of freshmen who have failed to properly disclose a large volume of stock trades are Rep. Pat Fallon, a Republican from Texas, and Sen. Tommy Tuberville, a Republican of Alabama.

Under the STOCK Act, members have 30 to 45 days after a stock trade to report when they, their financial advisor, or their spouse bought or sold stock. They must also disclose the name of the stock and list, within broad ranges, the value of any stock transaction.

If members don't report their trades on time, they're supposed to face a fine. But my Insider colleagues and I found such fines are rarely enforced in the House. Davis said he thinks the committee should take a harder look at penalties, which are supposed to start at $200 regardless of how late a member was in reporting the trades or how much their trades were worth.

In our call, Davis touted his past record on transparency when it comes to US House finances. A few years ago he was part of a working group that made it possible for the public to sort data about congressional office spending.

But the public database for searching House trades, while online, isn't sortable or searchable. And a database for reviewing financial trades of top congressional staffers isn't searchable, sortable or even online — one must physically go to the US Capitol to access it.

I asked Davis whether he'd ever tried to use the existing clunky system, and explained how difficult it had been for us reporters to cull the data for our "Conflicted Congress" investigation.

Davis sounded surprised, and said he hadn't tried to search the database to see what it was like.

"I will now that you brought it up," he said.

STOCK Act at 10: Lawmakers reflect on what worked — and what needs fixing — with Congress' conflicts-of-interest law

Mon, April 4, 2022, 4:30 AM

President Barack Obama signed the STOCK Act in 2012 to increase transparency of lawmakers' trades. But the enforcement system is a mess.AP/Charles Dharapak

- President Barack Obama signed the STOCK Act into law a decade ago.
- It was intended to increase transparency and curb personal financial conflicts of interest.
- But news investigations, including by Insider, reveal the law often fails to live up to its promise.

President Barack Obama signed the Stop Trading on Congressional Knowledge Act into law 10 years ago today, in a ceremony that marked a rare moment of bipartisanship during a midterm election year.

"It shows that when an idea is right that we can still accomplish something on behalf of the American people and to make our government and our country stronger," Obama said before taking up his presidential pen.

The law created new financial disclosure requirements and enforcement rules for members of Congress, their immediate families, and staff who decide to trade stocks. It clarified that insider trading was illegal on Capitol Hill. It defined how members of Congress could personally invest their money — and could not.

But in the months since Insider published "Conflicted Congress," an investigation into the personal finances of federal lawmakers, Congress is considering whether the

STOCK Act went far enough.

While current law allows members of Congress to trade individual stocks, Insider's "Conflicted Congress" investigation found that more than 1 in 10 lawmakers have recently violated the STOCK Act's disclosure provisions, which requires members of Congress to publicly report their trades shortly after making them.

The Insider investigation also exposed numerous conflicts of interest and instances where members of Congress' financial investments ran afoul of their policy positions.

For instance, members who hold stock in defense contractors also work on committees that have jurisdiction over military policy. Others who craft anti-tobacco policy have invested in tobacco giants. In the weeks immediately before and after the COVID-19 pandemic gripped the nation in March 2020, dozens of lawmakers bought or sold stock in companies that manufacture COVID-19 vaccines, treatments, tests, and personal protective equipment.


yahoo!finance
MORE CRYPTO
THAN YOU CAN HANDLE
(THAT'S A GOOD THING)
You won't run out of coins to track any time soon.
We've added 9k more to our coverage.
SEE IT ALL