SECURITIES LITIGATION UNIFORM STANDARDS ACT OF 1998

SPEECH OF

HON. EDWARD J. MARKEY

OF MASSACHUSETTS

IN THE HOUSE OF REPRESENTATIVES

Tuesday, July 21, 1998

Mr. MARKEY. Mr. Speaker, pursuant to the gentleman from Virginia's unanimous consent request of July 21, 1998 that all Members be given 5 legislative days within which to revise and extend their remarks on H.R. 1689 and to insert extraneous material, I wish to take the opportunity to extend upon my earlier remarks regarding this legislation and to respond to some rather incredible—and I believe inaccurate—remarks made by some of my distinguished colleagues regarding this legislation.

As I have indicated, I oppose this bill. If this bill is to become law, however, it is imperative that we clarify what the scienter requirement will be under the national standards created by H.R. 1689. My colleague from California—Representative Cox—seems to believe that standard should not include recklessness. I strongly disagree.

The federal courts have long recognized that recklessness satisfies the scienter requirement of Section 10(b) and Rule 10b-5—the principal antifraud provisions of the federal securities laws. It is true, as some of my colleagues have noted, that in Ernst & Ernst v. Hochfelder, the Supreme Court left open the question of whether recklessness could satisfy the scienter requirement of Section 10(b) and Rule 10b-5. My colleague from California, however, omits to state that the Court explicitly recognized that ''in certain areas of the law recklessness is considered to be a form of intentional conduct for purposes of imposing liability for some act.'' My colleague from California also neglects to state that since Hochfelder was decided, every court of appeals that has considered the question — ten in number — has interpreted the text of Section 10(b) and Rule 10b–5 to impose liability for reckless misconduct.

And these courts had good reason to so hold. Recklessness is vital to protect investors and the integrity of the disclosure process. Without liability for reckless misstatements, injured investors would be able to recover only if they were able to prove that a defendant had intentionally lied. This would enable defendants who deliberately disregarded available information to avoid liability for investor losses, and would encourage corporate chieftains to bury their heads in the sand.

The recklessness standard promotes meaningful disclosure. Our securities laws are premised on disclosure. Issuers of securities must make full and fair disclosure of material facts to investors when offering their securities. If issuers of securities are liable for misstatements and omissions only when they consciously make false disclosures, they will have less incentive to conduct a probing inquiry into any potentially troublesome areas they discover in the course of preparing their disclosure documents. The recklessness standard helps ensure that disclosure is thorough and meaningful because it encourages issuers to know what is taking place in their own companies.

Finally, the recklessness standard helps bring deliberate securities violators to justice by preventing them from hiding behind evidentiary hurdles. Proving a defendant's actual knowledge of fraud in a securities case is often not possible. Defendants in securities fraud cases do not as a matter of course admit their fraudulent intent. Proving actual knowledge is particularly daunting when, as is often true in securities cases, the evidence relating to the defendant's state of mind is entirely circumstantial. As the U.S. Court of Appeals for the Second Circuit—one of the ten courts of appeals to have put their stamp of approval on recklessness—has noted: ''Proof of a defendant's knowledge or intent will often be inferential . . . and cases thus of necessity [are] cast in terms of recklessness. To require in all types of 10b–5 cases that a factfinder must find a specific intent to deceive or defraud would for all intents and purposes disembowel the private cause of action under § 10(b).''

I do agree with my colleague from the state of California that the 1995 Private Securities Litigation Reform Act did not change the scienter requirement for liability. I am deeply troubled, however, by his attempt to attribute to the Reform Act Conference Committee—of which I was a member—an intention to raise the pleading standard beyond that of the Second Circuit—which, at the time of the Reform Act was the strictest pleading standard in the nation. That clearly was not my understanding nor my intent. Indeed, not only is my colleague attempting to revise history, he is doing so in a manner that would create an illogical result. Because the antifraud provisions allow liability for reckless misconduct, it follows that plaintiffs must be allowed to plead that the defendants acted recklessly. To say that defrauded investors can recover for reckless misconduct, but that they must plead something more than reckless misconduct defies logic.

Likewise, I must take strong exception to the suggestion of my colleague from California about the Conference Committee's intentions regarding a footnote in the Statement of Managers. That footnote, inserted at the last minute without my knowledge and without any discussion of the matter by the Members during the Conference Committee meetings, states that the Committee chose ''not to include in the pleading standard certain language relating to motive, opportunity, or recklessness.'' Contrary to my colleague's statements, this footnote—and make no mistake about it, that's all it is, merely a footnote—does not mean that recklessness has been eliminated either as a basis for liability or as a pleading standard. Existence of this footnote in no way mandates that courts not follow the Second Circuit approach to pleading. The Conference Committee and the Congress that passed the Reform Act also chose not to expressly include conscious behavior in the pleading standard. Yet surely no one would suggest that in doing so, the Conference Committee and Congress intended to eliminate liability for conscious misconduct.

My colleague points to the fact that the President vetoed the bill because of his concerns that the conferees intended to adopt a pleading standard higher than the Second Circuit's. Members in both the House and the Senate following the veto made clear that we did no more than adopt the Second Circuit standard. In this regard, I strongly agree with my colleague from California, Congresswoman LOFGREN, who stated in the legislative history following President Clinton's veto: ''The President says he supports the second circuit standard for pleading. So do I. That is what is included in this bill.''

I would suggest that it is the gentleman from California, rather than myself and other opponents of this legislation, that are trying to rewrite history. I continue to feel that both the Reform Act of 1995 and the present legislation are bad for investors and bad for our financial markets. We do not need to compound the harm done by this legislation with revisionist histories that seek to surreptitiously eliminate liability for reckless behavior.

DISAPPROVAL OF MOST-FAVORED-NATION TREATMENT FOR CHINA

SPEECH OF

HON. TIM ROEMER

OF INDIANA

IN THE HOUSE OF REPRESENTATIVES

Wednesday, July 22, 1998

Mr. ROEMER. Mr. Speaker, I rise in strong opposition to H.J. Res. 121, disapproving Most Favored Nation trading status with China. I rise in strong support of normal trade relations and continued constructive engagement with China. I support constructive engagement with China as a method of improving our critically important bilateral relationship and pursuing our foreign policy goals to advance human rights and religious freedom. While progress is at times slow and painful, talks and diplomacy are key aspects of this bilateral relationship.

Last year's trip by President Jiang Zemin to the United States to participate in the first U.S.-China Summit in a decade was the first step in achieving our goals through constructive engagement. President Clinton's highly successful trip to China last month demonstrated that constructive engagement is the most effective way to advance our national interests and promote our values. The United States is committed to improving human rights conditions in China, and I strongly believe human rights should remain a firm pillar of U.S. foreign policy.

Under our policy of constructive engagement, China has acted forthrightly to address our differences, including human rights, both privately and publicly, advancing American values and principles of freedom and democracy. Within the past year, Chinese authorities released numerous political dissidents including Wei Jingsheng and Wan Dan as well as religious leaders like Bishop Zhou. China also signed the United Nations Covenant on Economic and Social Rights and has pledged to sign the UN Covenant on Civil and Political Rights in the fall. This has resulted in meaningful improvements in the lives of millions of Chinese.

Despite official restrictions, the number of religious adherents in China is growing rapidly, with tens of thousands of churches, both registered and unregistered, and with tens of millions of worshipers. I am pleased that Presidents Clinton and Jiang agreed to continued exchanges among officials and religious leaders to improve our mutual understanding of the role of religion in each country. The Chinese government has hosted several delegations of U.S. and foreign religious leaders and the UN Working Group on Arbitrary Detention.