

What Constitutes Insider Trading?

[Dori Zinn](#) February 15, 2023

Buying and selling [shares of company stock](#) isn't illegal. But what about when you do it for a company you work for or otherwise interact with? Insider trading can be tricky. One wrong move can turn savvy trading into illegal trading. Here's the difference between good versus bad insider trading.

A [financial advisor](#) can help you understand the ins and outs – including legal boundaries – of trading when you have privileged knowledge of a company or its securities.

Insider Trading Defined

Insider trading is when a person has private knowledge about a company they own shares in and makes investing trades based on that knowledge. An insider can also pass along private knowledge about a company even if they don't own a stake in it but shares information with someone who does. If you make investment decisions based on knowledge that the public doesn't know, that's insider trading.

Insider trading in its most basic form isn't illegal. There's a difference between legal and illegal insider trading.

Legal Insider Trading

If insiders buy and sell stocks, they must register transactions with [the Securities and Exchange Commission \(SEC\)](#) through advanced filings. This kind of insider trading often goes unnoticed because it doesn't violate any rules.

When employees [buy stock from the company they work for](#) or CEOs [buy back their company shares](#), this is legal insider trading. As long as these

transactions happen through advanced SEC filings.

Illegal Insider Trading

Illegal insider trading is when you use private information to make trades for profit and don't disclose those trades through advanced SEC filings.

Anyone can commit illegal insider trading, not just someone who works at a company or has a working knowledge of a company. Common illegal insider trades can involve officers, directors and other company employees. But it also can involve friends of employees or others. If they receive private information about a company before the public knows about it, they could find themselves in trouble.

The SEC monitors illegal insider trading by watching trade volumes on companies. If a company's share volume fluctuates without news releases from or about the company, the typically SEC flags it. They'll usually investigate it further to see if shares changed hands illegally.

Handling Private Information Legally

If you've ever been tipped off about something before everyone else knew about it, that's not necessarily a bad thing. Many times, in many circles all over the world, [people share insider information](#). It's what you do with that information that matters.

If you find out that a company's earnings fell short of expectations before earnings are officially released, that's OK. But if you sell shares of that company after learning about those less-than-stellar earnings, or you pass that information on to someone who does, that's considered illegal insider trading.

If you make the sale after the earnings are released, you're not doing anything illegal since the earnings are considered public information and

everyone has access to the same information.

The Bottom Line

There's a fine line between right and wrong when it comes to illegal insider trading. It's not about what type of information you know, but rather, how soon you act on that learned information. Before you take any actions after you learn private information about a company, consider the potential consequences. Illegal insider trading is a felony even if you don't make a transaction yourself. It's against the law to pass along information used to make illegal insider trades later.

Anyone can run afoul of illegal insider trading. With information passed along from person to person, the SEC can trace back to those who originally shared the details.

Investment Tips

- If you aren't sure if you're conducting insider trading or just informed investing, consider speaking to a financial advisor. If you don't have a financial advisor yet, finding one doesn't have to be hard. [SmartAsset's free tool](#) matches you with up to three vetted financial advisors who serve your area, and you can interview your advisor matches at no cost to decide which one is right for you. If you're ready to find an advisor who can help you achieve your financial goals, [get started now](#)
- It's normal to want your money to work hard for you, especially in the stock market. You may want to learn every detail about every investment so you can maximize your earning power. But not [every stock or security](#) is right for you, nor do you need to take advantage of every new trend that comes your way. Before you jump onto something, review company history, breaking news and price points. What reason do you have for investing in it now? If you don't have a solid answer, you may want to take a few steps back and reconsider your move.

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