

WEDNESDAY, OCTOBER 12, 2016

PERSPECTIVE

Insider trading conviction likely to stick

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Last week, the U.S. Supreme Court heard oral argument in the closely watched *Salman v. United States*, the first time the court has addressed an insider trading case since 1997. A number of the justices appeared ready to affirm the 9th U.S. Circuit Court of Appeals' decision in *Salman*, which would hand the U.S. Department of Justice and the Securities and Exchange Commission a critical win on insider trading liability.

The Supreme Court is expected to address the "personal benefit" test that has puzzled practitioners and experts alike. Specifically, the court granted certiorari on the question of whether the personal benefit test articulated by *Dirks v. SEC*, 463 U.S. 646 (1983), requires proof that the tipper received a "tangible" or "pecuniary" gain from the tip, or whether it is enough that the insider and tippee shared a close family relationship.

Salman involves an intricate web of familial relationships, the facts of which allow the Supreme Court to address the personal benefit test head on. Bassam Yacoub Salman was convicted of insider trading in 2013 after making profits of approximately \$1 million on lucrative stock trades based on inside information he obtained from his future brother-in-law Mounir "Michael" Kara. The original tipper was Maher Kara, a Citigroup employee, who was Michael's brother.

The 9th Circuit affirmed the conviction based on *Dirks*, which held that an insider trading violation occurs "when an insider makes a gift of confidential information to a trading relative or friend." The 9th Circuit found no reason to diverge from *Dirks*, which it found to clearly encompass the facts of *Salman*.

In holding that no pecuniary or tangible benefit was necessary to prove a personal benefit, the 9th Circuit found itself in direct conflict with the 2nd U.S. Circuit Court of Appeals' holding in *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014). *Newman* requires the government to show a meaningfully close relationship between the tipper and tippee "that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature." Unsurprisingly, the Supreme Court granted certiorari to resolve the circuit split.

Justices Appear Unwilling to Ignore or Overturn *Dirks*

Interjecting quickly after *Salman*'s counsel began her argument, the justices seemed skeptical of the bright-line "pecuniary" benefit test she advocated. While counsel argued that no personal benefit was

obtained by the insider brother (other than possibly eliminating pressure from his brother's repeated requests for inside information), Justice Stephen Breyer noted that "to help a close family member is like helping yourself" and that the law is "filled with instances" in which providing a benefit to a close family member or friend is treated the same as providing benefit to yourself. Justice Anthony Kennedy agreed, pointing out that "you certainly benefit from giving to your family ... [because] ... it helps you financially because you make them more secure."

Turning to the "gift" language in *Dirks*, Justice Elena Kagan seemed to disagree with *Salman*'s proposed test because it required the court to "ignore some extremely specific language in *Dirks*." *Salman*'s counsel was unable to gain any ground by downplaying *Dirks*' "gift" language as dictum. Kagan even said, "I don't know what 'dictum' means. The court is very clearly setting out a test here. And [the gift language] is part of the test."

Several justices also appeared unmoved by another of *Salman*'s main arguments concerning the need for narrower insider trading liability considering the absence of guidance on insider trading within the statutory framework. Both Justices Sonia Sotomayor and Breyer noted that courts have been developing law to clarify statutes and undefined terms in a number of laws "over a long time." And Justice Kagan expressed concern that *Salman* was asking the court "to cut back significantly from something that we said several decades ago, something that Congress has shown no indication that it's unhappy with."

Justices Indicate Interest in Clarifying Personal Benefit Test

Despite appearing to favor the government's position, several justices also indicated an interest in using *Salman* as a springboard to reform or at least clarify the personal benefit test. The justices questioned government counsel on whether the *Dirks* test should be changed to illuminate the difference between a gift of inside information and a "casual social interchange."

In a related line of questioning, the justices also sought examples in which providing inside information to a family member or friend would not entail a personal benefit to the tipper. The government argued that there was a personal benefit any time the tipper provided the inside information to another when he or she knew that the other would trade on it, reasoning that the "advantage that you receive is that you are able to make a gift with somebody else's property." The justices seemed skeptical of this



The New York Times

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argument, which essentially eliminates the personal benefit requirement altogether.

The government concluded its argument by suggesting that the court need not go further than reaffirming *Dirks* (and thus, affirming *Salman*) if it felt comfortable with the *Dirks* test. Nonetheless, the government proposed a test that would replace an inquiry into personal benefit with an evaluation of whether there was a proper corporate purpose for the dissemination of nonpublic information.

Affirmance of *Salman* Appears Likely

With Justices Ruth Bader Ginsburg, Kagan, Sotomayor, Breyer and Kennedy asking questions that seem to favor affirming *Salman* and *Dirks*, it appears likely, at a minimum, that *Salman*'s conviction will be affirmed. These five justices looked to be strongly against the bright-line pecuniary benefit test that *Salman* offered.

What remains to be seen is what further guidance the Supreme Court will provide with respect to the personal benefit test — whether the *Dirks*' version of the test will be affirmed, reformed, clarified, or possibly (but much less likely) even eliminated. Notably, Justices Breyer and Kennedy, who are seen as more centrist members of the court, actively questioned the government about the constraints of the current personal benefit test any may temper any expansion of *Dirks* favored by other by members of the court.

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