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Unanimous Supreme Court Rejects Second Circuit's Limitations on Insider Trading Cases



For those watching in the trading world, the U.S. Supreme Court has confirmed that your friends can, indeed, pass on a gift of non-public information about a company that could leave you criminally liable for insider trading, even if they gain nothing concrete in return.

This morning the Supreme Court released its [unanimous opinion](#) in *Salman v. United States*, a closely-watched case that resolves a circuit split between the Ninth Circuit Court of Appeals and Second Circuit Court of Appeals and unwinds a Second Circuit decision that had imposed new requirements for insider-trading convictions. Specifically, the Supreme Court confirmed that in a prosecution against a "tippee" who received material inside information, prosecutors do not need to show that the tipper received a concrete benefit in exchange for the leak. The Supreme Court established the potential for tippee liability for insider trading over thirty years ago in *Dirks v. SEC*, 463 U.S. 646 (1983), a seminal decision in which the Court held that a tippee could be liable if the tippee knows inside information was disclosed in breach of the tipper's fiduciary duty. The Court further explained that a tipper breaches such a fiduciary duty when the tipper discloses information for a personal benefit, and that the jury could infer a personal benefit where the tipper receives something of value or "makes a gift of confidential information to a trading relative or friend." This framework was then used by lower courts and juries for decades in criminal and civil insider trading cases brought by prosecutors and the Securities and Exchange Commission. The *Salman* case involved an investment banker who passed on sensitive information about pending mergers and acquisitions to his brother, who then traded on that information and passed it on to others, including Salman. Salman was indicted in federal court in California, and was convicted of securities fraud in a jury trial in 2013 after the brothers (who both pleaded guilty) testified at Salman's trial. While Salman's appeal to the Ninth Circuit was pending, the Second Circuit issued its opinion in *United States v. Newman*, 773 F.3d 438 (2014), in which the Second Circuit reversed convictions of two portfolio managers who traded on insider information after finding that they were several steps removed from corporate insiders. Though the Second Circuit acknowledged that *Dirks* allowed a factfinder to infer a personal benefit to the tipper from a gift of information to a trading relative or friend, the Second Circuit had held that such an inference "is impermissible in the absence of proof of a meaningfully close personal relationship that generates an exchange that is objective, consequential, and

represents at least a potential gain of a pecuniary or similarly valuable nature." At the time and since, the *Newman* decision was viewed as establishing a new, heightened bar for prosecutors and the SEC considering insider trading cases against tippees, and in fact numerous convictions were overturned in the wake of *Newman*. On appeal to the Ninth Circuit, Salman had pointed to *Newman* to argue that his conviction should be reversed, asserting that there was no evidence that the tipper received anything of "a pecuniary or similarly valuable nature" in exchange for sharing information or that Salman knew of any such benefit. The Ninth Circuit rejected the argument and the decision in *Newman*, finding that it was governed by *Dirks*'s holding that a tipper benefits personally by making a gift of confidential information to a trading relative or friend. Salman renewed his arguments in the Supreme Court, which accepted the case after denying a prior request that it review the decision in *Newman*. He argued that an insider's gift of confidential information to a trading friend or relative is not enough to establish securities fraud, and that a tipper's goal in disclosing information must be to obtain money, property, or something of tangible value. But the Supreme Court disagreed, and held that its decision in *Dirks* "easily resolves the narrow issue" presented by the *Salman* case. The Supreme Court reaffirmed that disclosure of confidential information without personal benefit is not enough, but held that its discussion of "gifting" insider information in *Dirks* was dispositive. The Court emphasized that in *Dirks* it held that a personal benefit could be inferred when a tipper made a gift of information "to a trading relative or friend," and in *Salman* the tipper provided insider information to a close relative, his brother. The Court then explicitly held that the Second Circuit's suggestion that a tipper must receive something of a "pecuniary or similarly valuable nature" was inconsistent with *Dirks*. The Court also rejected Salman's argument that the gift-giving standard in *Dirks* is unconstitutionally vague, finding instead that it created a "simple and clear 'guiding principle' for determining tippee liability." The decision is the first Supreme Court decision in an insider trading case in decades, and likely will have an immediate and significant impact on prosecution decisions in the Second Circuit and elsewhere. By any measure, it is a big win for the government, and leaves prosecutors and the SEC with considerable discretion in making decisions on the appropriate scope of insider trading enforcement, an area that has been a high priority of both the DOJ and SEC for years. However, practitioners and traders who had appreciated the Second Circuit's effort to clarify the requirements for insider trading will view the "simple and clear" guidance from the Supreme Court in *Dirks* and now *Salman* as anything but. As the Supreme Court itself acknowledged, because it viewed *Salman* as involving "precisely" the situation that *Dirks* envisioned, there was no need for it to address the "difficult questions" that might arise in other factual circumstances.

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