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Unanimous Supreme Court Decision Will Significantly Increase the Ability of Federal Prosecutors to Pursue Certain Insider Trading Cases

Action Item: Last week, in a unanimous decision in *Salman v. U.S.,* the U.S. Supreme Court affirmed the Ninth Circuit's interpretation of insider trading rules, permitting prosecutions even when the insider/tipper did not personally receive money or property in exchange for the tips. *Salman v. United States,* No. 15-628, 2016 WL 7078448, at *1 (U.S. Dec. 6, 2016). In doing so, the Court rejected the Second Circuit's 2014 decision in *U.S. v. Newman,* which precluded a factfinder from inferring a personal benefit to the tipper from a gift of confidential information to a trading relative or friend, unless the tipper received something in exchange of a "pecuniary or similarly valuable nature." 773 F. 3d 438, 452 (2014), *cert. denied* 577 U.S. ___ (2015).

In *Salman,* the defendant Bassam Salman, a grocery wholesaler from Chicago, traded on inside information he received from a friend, Michael Kara, who, in turn, received the information from his brother, Maher Kara, a former investment banker at Citigroup. Maher was also Salman's brother-in-law. While Maher eventually became aware that his brother Michael was trading on the inside information, he did not know that Michael was feeding that information to others—including Salman. Salman, who made over $1.5 million in profits from the tips, was convicted of securities fraud (insider trading) and sentenced to three years in prison and over $730,000 in restitution.

Salman relied on *Newman* to argue that his conviction should be reversed, because there was no evidence that Maher, who had made a gift of confidential information, received something of a "pecuniary or similarly valuable nature" in exchange. The Court dismissed Salman's arguments, agreeing instead with the Government's position that the precedent set by *Newman* was inconsistent with the controlling insider trading case, *Dirks v. SEC,* 463 U.S. 646 (1983). Justice Samuel Alito, writing on behalf of the Court, explained that *Dirks,* "makes clear that a tipper breaches a fiduciary duty by making a gift of confidential information to 'a trading relative.'" *Salman,* 2016 WL 7078448, at *8. This is so, because "giving a gift of trading information is the same thing as trading by the tipper followed by a gift of the proceeds." *Id.* Thus, to the extent *Newman* also requires the tipper to receive money or something similarly valuable in exchange for a gift to a relative or a friend, that requirement is "inconsistent with *Dirks.*" *Id.*

Under what the Court described as the "commonsense point we made in *Dirks,*" "[m]aking a gift of inside information to a relative like [in *Salman*] is little different from trading on the information, obtaining the profits, and doling them out to the trading relative." *Id.* Indeed, the jury could "infer that the tipper meant to provide the equivalent of a cash gift." *Id.* Thus, in *Salman,* Maher Kara breached his duty of trust and confidence to Citigroup when he gave information to his brother, Michael, knowing that Michael would trade on it; Salman acquired and breached that same duty when he traded on the information knowing that it had been improperly disclosed. *Id.*

Although the Court noted that the issue presented in *Salman* was a "narrow" one (id.), the *Salman* decision is a big win for the Government and will return federal prosecutors to where they were pre-Newman.

Prior to the *Salman* ruling, prosecutors in the Second Circuit (which includes the Southern District of New York, where a significant number of insider trading cases are prosecuted) were bound by the *Newman* decision. *Newman* had increased the evidentiary burden necessary to establish a tipper's fiduciary breach and resulting liability, and was viewed by prosecutors as a decision that, "will dramatically limit the Government's ability to prosecute some of the most common, culpable, and market-threatening forms of insider trading." Petition of the United States of America for Rehearing and Rehearing *En Banc, U.S. v. Newman,* 773 F.3d 438 (2d Cir. 2014) (No. 13-1837(L)), 2015 WL 1064423, at *13, *3 (Jan. 23, 2015).

In fact, after the *Newman* decision, the U.S. Attorney for the Southern District of New York announced that he was dismissing charges against one defendant, who was previously convicted at trial of insider trading, and six cooperating witnesses who had pled guilty, because those convictions could not stand under *Newman.*

Now, as a result of the *Salman* ruling, the Government can resume prosecutions of insider trading cases involving remote tipees. But only time will tell whether *Salman* will embolden prosecutors to pursue a greater number of insider trading cases. □

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