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The Supreme Court Limits *Newman*, but the Government Still Faces Obstacles in Insider Trading Cases

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White Collar Defense and Investigations

On December 6, 2016, in the first insider trading case the Supreme Court has decided in nearly two decades, the Court, in *Salman v. United States*, unanimously upheld a conviction for trading based on material non-public information provided by the defendant's brother-in-law as a gift.[1] The decision was a big win for the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC), in that it overruled a key aspect of the Second Circuit's 2014 decision in *United States v. Newman*,[2] which had curtailed the government's ability to bring insider trading cases when the insider did not financially benefit from passing the confidential tip. In so doing, *Salman* reaffirmed the continuing validity of a central holding in the Supreme Court's 1983 decision in *Dirks v. SEC*—that liability can exist when "an insider makes a gift of confidential information to a trading relative or friend."[3] Nonetheless, because the Court decided *Salman* narrowly, it left in place legal hurdles that the DOJ and the SEC may have trouble clearing if they continue to bring far-reaching insider trading cases, especially those involving multiple tiers of tippees.

In his opinion for the Court in *Salman*, Justice Alito viewed the basic fact pattern—the passing of information to a close relative—as an easy case, "in the heartland of *Dirks*'s rule concerning gifts."[4] Since the Ninth Circuit had reached the same result below, the Supreme Court appears to have taken the case solely to reject a more restrictive interpretation of *Dirks* adopted by the Second Circuit in *Newman*, which had held that, to create insider trading liability, tippers had to receive a tangible benefit in return. In *Salman*, the Supreme Court made clear that liability can apply when an insider passes a "gift" of confidential information to a "trading relative or friend," whether or not the insider receives a pecuniary benefit.[5]

The government immediately hailed *Salman* as a green light "to continue to aggressively pursue illegal insider trading and bring wrongdoers to justice."[6] And for good reason. With *Salman*, the

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[1] *Salman v. United States*, No. 15-628, 2016 WL 7078448 (U.S. Dec. 6, 2016).
[2] *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014), *cert. denied*, 136 S. Ct. 242 (2015).
[3] *Dirks v. SEC*, 463 U.S. 646, 664 (1983).
[4] *Salman*, 2016 WL 7078448, at *9.
[5] *Id.* at *7 (emphasis removed) (quoting *Dirks*, 463 U.S. at 664).
[6] Aruna Viswanatha & Brent Kendall, *Supreme Court Hardens Stance on Insider Trading*, Wall St. J. (Dec. 6, 2016), http://www.wsj.com/articles/supreme-court-backs-prosecutors-over-tips-from-friends-and-family-in-insider-trading-cases-1481038798 (quoting SEC Chair Mary Jo White); *see also* Statement of U.S. Attorney Preet Bharara on the Supreme Court's Decision in *Salman v. U.S.* (Dec. 6, 2016),

Court has brought within the reach of the insider trading laws a wide range of motivations typically at play when information is disclosed for non-corporate purposes. The government often will be able to fit its insider trading cases into one of the *Salman*-approved boxes: an insider either seeking to benefit himself financially, or trying to help a friend or relative.

Yet *Salman* does contain some signals that the Supreme Court would reject efforts to stretch the definition of relative or friend too far. Throughout the opinion, the Court is careful to note how "very close" the insider was with the initial tippee.[7] The insider not only "love[d] [his] brother very much," but thought of him as "a second father" and wanted to "help him" to "fulfil[l] whatever needs he had."[8] Thus, while *Salman* certainly approves of liability for disclosures to a "close relative," it and other courts may be reluctant to extend it to more distant acquaintances or relatives.

Moreover, despite freeing the government from some of *Newman*'s restrictions, *Salman* still leaves doors open for the defense. For example, under *Newman*, the government must prove that a downstream tippee knew that the original breach was in return for a benefit.[9] That requirement was not at issue in *Salman* and was not questioned in the Supreme Court's decision. Nor does *Salman* resolve how consequential a benefit to an insider must be in cases not involving a gift of information to a relative or friend. Indeed, quoting *Dirks*, *Salman* reiterated that "'[d]etermining whether an insider personally benefits from a particular disclosure, a question of fact, will not always be easy for courts.'"[10] In short, the battle over the scope of insider trading law, though moving to new fronts, is far from over.

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https://www.justice.gov/usao-sdny/pr/statement-us-attorney-preet-bharara-supreme-court-s-decision-salman-v-us.

[7] *Salman*, 2016 WL 7078448, at *4.

[8] *Id.* (alterations in original).

[9] *Newman*, 773 F.3d at 448; *United States v. Rajaratnam*, 802 F. Supp. 2d 491, 498-99 (S.D.N.Y. 2011); *State Teachers Ret. Bd. v. Fluor Corp.*, 592 F. Supp. 592, 594 (S.D.N.Y. 1984).

[10] *Salman*, 2016 WL 7078448, at *11 (alteration in original) (quoting *Dirks*, 463 U.S. at 664).