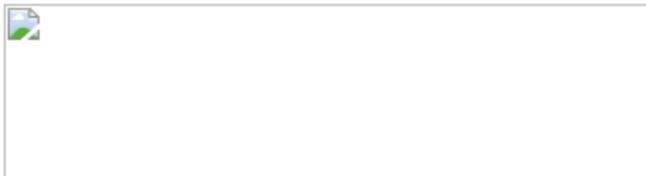


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Subject: Fwd: Supreme Court Rejects Newman Requirement
Date: Thu, 08 Dec 2016 15:22:11 +0000



SECURITIES LITIGATION ALERT

DECEMBER 7, 2016

Supreme Court Rejects Newman Requirement of "Pecuniary or Similarly Valuable" Personal Benefit for Insider Trading Liability for Tipping Family and Friends

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The U.S. Supreme Court gave the government a major victory in *Salman v. U.S.*,^[1] which lowers the standard for proving insider trading involving tipping family or friends, and will embolden the government to bring similar cases. *Salman* holds that a gift of inside information to a family or friend is sufficient to prove insider trading tipping liability - even if the tipper did not receive a valuable *quid pro quo* in exchange for the tip. This significantly narrows *U.S. v. Newman*, in which the Second Circuit (a lower appellate court) held that a tipper must receive "at least a potential gain of a pecuniary or similarly valuable nature," as a personal benefit necessary to be held liable for insider trading.^[2] *Salman* will almost certainly embolden the SEC and federal prosecutors to bring more insider trading cases, because it is much easier for the government to prove a "gift" to a "friend" than to prove a "pecuniary" or similar *quid pro quo*.

In *Salman*, an investment banker at Citigroup tipped his Brother about certain pending healthcare mergers involving Citigroup clients. The Brother traded on that information for a profit, and also tipped his Brother-in-Law, Mr. Salman, who also traded for a profit. At trial, the government relied solely on the tippers giving a gift of inside information to a close family member to satisfy the "personal benefit" requirement of tipper-tippee insider trading liability. The government did not identify any money or other valuable *quid pro quo* paid for the tip. *Salman* was convicted at trial, and his conviction was upheld by the Court of Appeals for the Ninth Circuit.

The Supreme Court affirmed *Salman's* conviction, holding that a gift of inside information to family or friends is sufficient to prove a "personal benefit" for insider trading tipping liability. The Court reasoned that such a gift can be inferred to "provide the equivalent of a cash gift."^[3] Specifically, the Court reasoned that if the tipper personally traded on inside information himself for a profit, but gave the proceeds to his brother, the tipper receives a personal benefit (cash) and is liable for insider trading. So, it reasoned, where a tipper achieves effectively the same result by gifting the information to his brother with the expectation that the brother will trade on the information to obtain a cash profit, the result should be the same.

Importantly, the Supreme Court explicitly stated that it was narrowing the Second Circuit's landmark *Newman* decision. It stated, "[t]o the extent the Second Circuit held that the tipper must also receive something of a 'pecuniary or similarly valuable nature' in exchange for a gift to family or friends,... we agree with the Ninth Circuit that this requirement is inconsistent with *Dirks*," a prior Supreme Court ruling.^[4] This significantly lowers the standard of proof for insider trading tipping liability in cases involving family or friends. The government often cannot find evidence of money or a similarly valuable *quid pro quo* between the tipper and tippee in insider trading cases. So it is much easier to prove a case of insider trading by arguing that the exchange of information was a "gift," which essentially only requires some evidence (even circumstantial evidence such as phone logs) that the tipper gave information to the tippee.

So where does this leave the *Newman* decision? The *Newman* decision itself was not overturned by the Supreme Court, because *Newman* also relied on the lack of proof that the tippees who traded on inside information knew that the tippers provided inside information in exchange for a personal benefit - especially since the tippees were several steps removed from the original tippers. In addition, *Newman's* "pecuniary or similarly valuable" benefit test should still apply to cases that do not involve tipping family or friends.

Nevertheless, the *Salman* decision tips the scales back in favor of the government in tipping insider trading cases. The SEC and federal prosecutors have shown in the past that they will bring cases based on alleged gifts of inside information to mere social acquaintances, fellow employees, or networking contacts - using strained arguments of "friendship." And they will bring insider trading cases based solely on circumstantial evidence (*e.g.*, a pattern of phone calls) where there is no direct proof of trading based on inside information. Accordingly, with *Salman* imposing a lower standard of proof, it is imperative that clients contact counsel immediately at the first hint of a government insider trading investigation.

[1] *Salman v. U.S.*, No. 15-628, 580 U.S. ____, slip op. (Dec. 6, 2016).

[2] 773 F.3d 438, 452 (2d Cir. 2014).

[3] *Salman*, Slip Op. at 9-10.

[4] *Id.* at 10.

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