

Justices Look Past Newman To Address Insider Trading Split

By Ed Beeson

Law360, New York (January 19, 2016, 10:05 PM ET) -- After snubbing prosecutors last fall when it rejected their appeal of the landmark Newman decision on insider trading, the U.S. Supreme Court on Tuesday showed it just wanted a better case when it accepted another matter involving a question about what benefits need to be exchanged to make trading on confidential tips illegal.



The insider trading case involving Bassam Salman presents an opportunity for the U.S. Supreme Court to rectify what many have said is an emerging circuit split over what counts as a personal benefit. (Credit: Law360)

This latest case involves Bassam Salman, an Illinois man convicted of trading on tips that made their way to him from his future brother-in-law, a former Citigroup banker. He has claimed that a California federal appeals court broke with the Second Circuit when it found it sufficient to show that rather than receive something in return, the banker had made a gift of his tips to his brother, and they in turn were passed to Salman.

The matter presents an opportunity for the Supreme Court to rectify what many, including the federal government, have said is an emerging circuit split over what counts as a personal benefit, a central piece of establishing tipper liability ever since the Supreme Court handed down its seminal 1983 decision known as *Dirks*.

The high court previously had the opportunity to resolve this split when U.S. Solicitor General Donald Verrilli presented an appeal of the Second Circuit's Newman decision, which raised the bar on the

government by holding that prosecutors must show that tippers got at least a potentially pecuniary benefit for their confidential information. But the justices passed on the chance in October when they summarily denied the petition for certiorari without comment.

The following month, Salman submitted what many saw as a long-shot petition for certiorari. At the time, his attorney argued his case was the “ideal vehicle” for resolving the circuit split that Verrilli first raised before the court.

Attorneys say they now see why.

“The Salman case is a cleaner case in which the court can clarify the personal benefit standard,” said David I. Miller, a partner at Morgan Lewis & Bockius LLP and former federal prosecutor.

Among other things, the high court won’t have to contend with the possibility that no matter how it rules, Salman will be left unaffected. That was a real possibility the court faced if it had taken up the Newman decision. Attorneys for at least one of the former hedge fund managers at the heart of the case told the justices that the men would still go free even if Newman were reversed.

The reason why had to do with the fact that the government only appealed half of the Newman decision. In its December 2014 decision, the Second Circuit stated the government also had to show that tippees knew of the exchange of personal benefits for confidential information they traded on. As so-called downstream tippees, Todd Newman and Anthony Chiasson were too far removed from the original sources of inside information to have any knowledge of their tipper, their attorneys argued.

By contrast, a Supreme Court ruling would have bearing on Salman’s fate, his attorney argued. If the court were to find that a close family relationship is enough to establish a personal benefit, “then Salman loses,” he said in his certiorari petition. But if the court decides there must be an “objective, consequential” and potentially pecuniary benefit traded for confidential information, “then Salman prevails.”

A jury convicted Salman in September 2013 on charges that he reaped more than \$1.5 million in illegal profits through trades he set up another relative to make.

In his appeal to the Ninth Circuit, Salman sought to leverage Newman by arguing there was no evidence to prove the former Citigroup banker, Maher Kara, got a tangible benefit for passing insider information to his brother Michael Kara.

“To the extent Newman can be read to go so far, we decline to follow it,” the Ninth Circuit said in response.

Miller said it would be “pretty dramatic” if the high court did not affirm Salman’s conviction. Michael and Maher Kara both pled guilty to conspiracy and securities fraud in July 2011 while the relative who allegedly helped Salman trade his inside information, Karim Bayyouk, was convicted in 2013 and later sentenced to 18 months in prison. Salman himself was sentenced to three years in prison.

“Hopefully now we will finally get some level of clarity about what does constitute a personal benefit once and for all,” he also said.

It’s impossible to know how the justices will ultimately rule on Salman, but it could be telling that they

rejected the petitioner who asked for looser standards around insider trading law, notes Michael Friedman, general counsel with Trillium Management LLC and a former Winston & Strawn LLP partner.

“The guy asking for stricter definition got more favor with the Supreme Court,” he said.

The high court may also have taken issue with aspects of the Ninth Circuit’s decision, which was written by the U.S. District Judge Jed S. Rakoff, the Manhattan jurist who sat on the panel by designation.

Pointing to language in Judge Rakoff’s opinion that says it is sufficient to show that an insider tipped with the intent to benefit a trading relative or a friend, “that’s too blanket of a license to the government,” Friedman said.

The language on making gifts of inside information to a trading relative or a friend arises from the Dirks decision. Taking up the Salman matter now gives the high court a chance to revisit, tweak and possibly overhaul the standard that’s been on the books for a third of a century.

In fact, re-evaluating Dirks is probably the first step the court takes before it tackles the Salman decision and by extension Newman, said Jonathan Richman, co-head of the securities litigation group at Proskauer Rose LLP.

“What does the court do with Dirks? Does it keep it? Does it retreat from it? Or does it change it?” he said. “Everything is up for grabs now.”

The court could also rule in a way that affects the holding in Newman as it relates to more remote tippees.

“It’s possible they could say something that doesn’t necessarily undermine the Newman decision but ultimately narrows it,” Miller said.

Whether the eventual decision is more helpful to prosecutors like U.S. Attorney Preet Bharara, for whom Newman was a big setback, or to insider trading defendants remains to be seen.

But either way the court comes out, it will be better to have one clear standard than a brew of potentially conflicting ones bubbling up around the country, legal experts say.

“When the line is not clear, everybody is in a difficult position,” said Jonathan Schmidt, a former federal prosecutor who is now a Ropes & Gray LLP counsel.

Salman is represented by John D. Cline of the Law Offices of John D. Cline.

The U.S. is represented by U.S. Solicitor General Donald Verrilli.

The case is Salman v. U.S., case number 15-628, in the U.S. Supreme Court.

--Editing by Jeremy Barker and Christine Chun.
