

Appeals Courts Still Lost In Post-Newman Trading Muddle

By **Carmen Germaine**

Law360, New York (May 27, 2016, 11:48 PM ET) -- The First Circuit's Thursday decision upholding a Massachusetts attorney's conviction for trading on tips from a golf buddy widened a circuit split in the wake of the Second Circuit's Newman decision and showed that courts are waiting for the U.S. Supreme Court to chip them back onto the fairway in insider trading law, experts said.

In confirming Lowell, Massachusetts-based lawyer Douglas Parigian's insider trading conviction, a three-judge First Circuit panel nodded to the Second Circuit's 2014 decision in *United States v. Newman* and imposed a higher legal standard for criminal prosecutions. However, the panel said it can't go against the First Circuit's own more lenient precedent even as the Supreme Court mulls another case over what constitutes the personal benefit required to prove insider trading liability.

"How this will all play out, we do not venture to say because, as a three-judge panel, we are bound to follow this circuit's currently controlling precedent," Judge William J. Kayatta Jr. wrote for the panel.

Prosecutors alleged that Parigian traded on tips that a golfing buddy, Eric McPhail, received from an insider at American Superconductor Corp. and passed on through an email chain to a circle of friends. McPhail and Parigian were both criminally indicted, while the other tippees, including Holland & Knight LLP tax partner Douglas Clapp, were only hit with civil claims from the U.S. Securities and Exchange Commission.

Parigian pled guilty to the charges under a conditional agreement that allowed him to challenge his indictment at the First Circuit, where he argued that prosecutors failed to meet the Second Circuit's higher standard when they accused him of offering to buy a golf buddy dinner at a ritzy Boston steakhouse in exchange for insider information he traded on, court records show.

Because he never actually bought the dinner, Parigian argued, McPhail could not have received the benefit required. The panel disagreed, however, saying that McPhail and Parigian's relationship as "reasonably good friends" along with the promise of "various tangible luxury items" appeared to be enough under prior First Circuit precedent.

While the panel didn't say how it might have ruled with a different precedent, it did recognize that the Second Circuit's Newman decision applied a "more discriminating definition" of personal benefit and suggested that the Supreme Court could come to a different conclusion as it reviews the issue.

"This is kind of the First Circuit crying out in pain, 'Please relieve us from this confusion and complexity;

please provide us with some guidance,” said Stephen Crimmins, a partner at Murphy & McGonigle PC.

The decision adds to a growing circuit split, as the First Circuit noted that its holding aligns more closely with the Ninth Circuit’s decision in *United States v. Salman*, the case currently on appeal to the Supreme Court after the high court declined to review Newman. In that case, Bassam Salman has asked the high court to overturn his conviction, arguing that prosecutors need to show that the tipper received a monetary or property benefit in exchange for the tips.

“The Newman, Parigian and Salman decisions demonstrate the need for clarity here,” former federal prosecutor David I. Miller said.

Attorneys said that the First Circuit’s decision widens the split among appellate courts and signals that courts will continue to grapple with the personal benefits issue until the Supreme Court or Congress weighs in.

“Things are clear as mud,” said Stephen L. Hill Jr., a Dentons partner and former Missouri U.S. attorney.

Hill added that the developing split will mean that venue becomes as important as the underlying facts in future insider trading cases as prosecutors grapple with diverging instructions. Attorneys and courts alike are trained on the high court, waiting to see how much a future decision in the *Salman* case alters the insider trading landscape. Until that happens, both prosecutors and defense attorneys will continue to struggle with the complicated legal knot, according to Hill.

“If there’s one thing prosecutors and attorneys agree on, it is the benefit that comes from clearly understanding what all the requirements are going to be and the related evidence necessary to prove that,” he said.

Thursday’s decision could also play a part in the *Salman* case. *Salman* filed his opening brief earlier this month, but the government won’t file a reply until August.

“This is a major intervening decision, so it’s very possible the government might rely on and/or cite to this decision in its brief to the Supreme Court,” Miller said.

Miller, now a partner at Morgan Lewis & Bockius LLP, also warned that even the Supreme Court’s eventual decision in the *Salman* case may not bring the kind of clarity courts are hoping for if the justices opt to decide the case narrowly, which would be more likely if the court doesn’t get a ninth member before it issues a decision.

Although Miller had doubted the high court would decline to address the Newman decision and the circuit split, he noted that the *Salman* case offers a relatively clear question of personal benefit because the prosecutors’ case relied solely on the relationship between *Salman* and his two brothers-in-law, one of whom provided tips to the other for no tangible benefit.

“While the court could make it crystal clear that under *Salman*’s facts, a personal benefit has been provided, the court may not provide a categorical rule as to what constitutes a personal benefit in any situation,” Miller said.

Even if the Supreme Court does rule conclusively on what constitutes a personal benefit, attorneys said the First Circuit’s decision shows that insider trading has other kinks that still need ironing out.

Crimmins, a former SEC attorney, noted that Parigian was charged under the “misappropriation” theory of insider trading, meaning prosecutors alleged McPhail misappropriated information from an insider who expected him to keep it confidential. The Salman and Newman cases, meanwhile, were both based on a classical theory, under which the insider is alleged to have supplied information knowing the tippee would trade.

The First Circuit said that it’s unclear whether prosecutors even need to prove a personal benefit was exchanged in a misappropriation case and notably concluded that the benefits Parigian promised McPhail were enough “if a benefit is required.”

“What do you do if you have the other kind of insider trading case where an outsider is allegedly stealing the information? Do you still have to show personal benefit? Should you have to show personal benefit? That is still unclear,” Crimmins said.

And the panel’s focus on how the indictment was written and structured suggests other potential areas of contention, according to Hill.

“They certainly signaled that there was a value in taking a hard look at how the indictment had been set up,” he said.

The decision found Parigian had waived any claim that the indictment inconsistently alleged mens rea by sometimes claiming he “knowingly and willfully” committed securities fraud and suggesting in other instances that he “knew or should have known” that he was trading on material inside information. But the panel spent six pages in a 23-page opinion weighing the argument — twice the amount of space it devoted to examining the personal benefit issue — and said that if Parigian had raised the issue earlier, “he would have had a point.”

And in the meantime, McPhail, who was convicted at trial and sentenced to 18 months in prison, has also appealed to the First Circuit. Oral argument for McPhail’s case is scheduled for June 6.

“We’re in a very interesting time in the development of the law of insider trading,” Crimmins said. “It has achieved an incredible complexity as a result of case-by-case developments over 50 years.”

Representatives for the parties didn’t immediately respond to requests for comment late Thursday.

U.S. Circuit Judges William J. Kayatta, Norman H. Stahl and David J. Barron sat on the panel that reached Thursday’s decision.

The government is represented by Andrew Lelling.

Parigian is represented by Allison Koury.

The case is USA v. Parigian, case number 15-1994, in the U.S. Court of Appeals for the First Circuit.

--Additional reporting by Kat Greene and Max Stendahl. Editing by Christine Chun and Kat Laskowski.
