

Bharara's Newman Appeal Faces Steep Odds In 2nd Circ.

By **Ed Beeson**

Law360, New York (January 26, 2015, 9:58 PM ET) -- U.S. Attorney Preet Bharara likely will be given another shot at telling a federal appeals court why the government was correct to bring insider trading charges against a pair of hedge fund managers, but convincing the Second Circuit to reverse or even narrow the unanimous ruling of three of its judges will be a stiff challenge, attorneys say.

In a widely expected move, the top prosecutor in the Southern District of New York on Friday asked the appeals court to grant his office's requests for a rehearing and en banc review of a Dec. 10 decision that overturned the convictions and dismissed the indictments against Todd Newman and Anthony Chiasson, two hedge fund chiefs who had been accused of collectively scoring tens of millions of dollars in illegal profits by trading on inside information on Dell Inc. and Nvidia Corp. stock.

The petition said the court not only went against precedent in defining the personal benefits a tipper must receive in exchange for inside information but also refused to consider the evidence the government put forth about the benefits the tippers received in the Newman and Chiasson cases. Lastly, the government argues that the Second Circuit put investor confidence at risk of deep harm because of a loophole the decision created for would-be inside traders to exploit.

Given these extraordinary circumstances, as well as the fact that the U.S. Solicitor's Office and the U.S. Securities and Exchange Commission separately threw their weight behind Bharara's appeal, attorneys say they expect the whole court will take a rare step in this instance and give the matter further consideration.

"Petitions are generally not granted, but in important cases like this it is possible that the circuit will grant and rehear it," said David Miller, a partner at Morgan Lewis & Bockius LLP and a former federal prosecutor who beat a Second Circuit appeal by Winifred Jiau, a former technology consultant convicted at a related insider trading trial.

One of the arguments that may compel the Second Circuit to act on the government's petition, attorneys said, is the notion that the original panel of judges failed to give the government the opportunity to retry its case after it modified two key standards prosecutors must prove in insider trading cases: the personal benefits tippers receive for their information and the knowledge that tippers have of this benefit.

Under the court's analysis, to prove illegal tipping took place, the government must show that the tipper received something of at least possibly pecuniary or of some similar value, while tippers must know

about this benefit.

Both standards make it much more difficult for the government to prosecute insider trading in many scenarios, especially when it comes to so-called remote tippees who are several steps removed from the original source of information, attorneys said.

But trying to take on both issues in an appeal would make an incredible challenge even steeper. To this end, it appears the government is willing to concede the question about what tippees know about the benefits tippers receive for their information. In the opening of their petition, prosecutors called this “a requirement the government argued against but does not challenge herein.”

Instead, the government’s focus appears to be now more on the question of what counts as a benefit, as the Second Circuit flatly dismissed the softer exchanges, such as a deeper friendship, that have been at the heart of many insider trading claims.

“The bigger concern seems to be more the narrower interpretation of personal benefit than we’ve seen in these cases,” said Adam Pritchard, a University of Michigan Law School professor.

In pressing their claim for an en banc rehearing, prosecutors picked apart the appellate panel’s analysis of the U.S. Supreme Court’s landmark 1983 decision on insider trading, *Dirks v. SEC*, which established the requirement that there be a benefit exchanged. Prosecutors said the appellate panel ruling was “flatly inconsistent” with the high court precedent.

In looking back on the ruling, which cleared a securities analyst of illegal tipping when he disclosed a fraud inside his firm to investor clients but sought nothing in return, the Second Circuit “added an unprecedented limitation that effectively upended *Dirks*” by introducing language on pecuniary benefits, prosecutors said Friday.

The *Dirks* ruling specifically held that a benefit can be gift of confidential information to a trading relative or a friend, prosecutors noted. But the appellate panel took the benefit question in a different direction when it established a five-point test to be met before the “deliberate transmission of valuable inside information” to a friend or family member becomes a crime, prosecutors said.

The government said that under the previous standard for determining personal benefits, it had presented more than enough evidence to show that the corporate insiders whose tips became the foundation for Newman and Chiasson’s lucrative trades benefited from providing the information, such as by building relationships in hopes of career advancement.

But it’s an open question whether the rest of the appellate court will be convinced the personal benefit criteria are out of line with case law. Stuart Glass of Choate Hall & Stewart LLP said he is not sure the court will take a different track than the deliberate and unified approach the panel took last month.

“It will surprise me if this gets flipped,” he said.

But, he added, Bharara’s office has little to lose in pressing its claim.

“They’re going to take any avenue they can to try and get the decision narrowed,” Glass said. “They’re not going to get worse than what they have.”

Newman is represented by Stephen Fishbein and John Nathanson of Shearman & Sterling LLP. Chiasson is represented by Gregory Morvillo of Morvillo LLP, Mark Pomerantz of Paul Weiss Rifkind Wharton & Garrison LLP and Alexandra A.E. Shapiro of Shapiro Arato & Isserles LLP.

The government is represented by Sarah McCallum, Robert Allen, Harry Chernoff and Michael Levy.

The case is U.S. v. Newman et al., case number 13-1837, in the U.S. Court of Appeals for the Second Circuit.

--Editing by Kat Laskowski and Brian Baresch.

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