

Insider Trading Update: Department of Justice Seeks Supreme Court Review of Second Circuit Case Deciding Reach of Insider Trading Law

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The United States Department of Justice has petitioned the United States Supreme Court to review a recent Second Circuit opinion¹ that clarified what the Government must prove to establish an insider trading violation. Although the Second Circuit reaffirmed that the Government must prove that a corporate insider personally benefited from his disclosure, the court also held that inferring such a benefit from personal relationships is impermissible “in the absence of proof of a meaningfully close personal relationship that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature.” The Department of Justice argues that the Second Circuit’s definition of personal benefit unduly limits the reach of insider trading law, contravenes a prior Supreme Court decision, is in conflict with decisions by other courts of appeals, and will harm the securities markets. Importantly, the Department of Justice does not contest the Second Circuit’s other key ruling that required the Government to prove that a tippee knows of the personal benefit that the insider received in exchange for disclosure.

Background of the *Newman* Decision

Todd Newman, a portfolio manager at Diamondback Capital Management, LLC, and Anthony Chiasson, a portfolio manager at Level Global Investors, L.P., were convicted of securities fraud and conspiracy to commit securities fraud by a jury in the U.S. District Court for the Southern District of New York on December 17, 2012. At trial, the Government presented evidence that defendants were remote recipients of inside information acquired by a group of financial analysts who received information from insiders at Dell and NVIDIA.

Newman and Chiasson appealed to the U.S. Court of Appeals for the Second Circuit, which vacated their convictions. The Second Circuit’s opinion made two key rulings on the reach of insider trading law. First, the court held that a remote tippee must know that an insider received a benefit in exchange for his disclosure. Because the trial court did not instruct the jury that the Government needed to prove that Newman and Chiasson *knew* that the insiders received personal benefits for their disclosures, the appellate court found that their trial was defective.

Second, the court held that the Government’s evidence of the insiders’ friendship with the tippees was insufficient to meet the “personal benefit” requirement because inferring a benefit from personal relationships is impermissible “in the absence of proof of a meaningfully close personal relationship that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature.” The court further found that the Government had provided no

¹ See [United States v. Newman](#), 773 F.3d 438 (2d Cir. 2014). For further analysis of the Second Circuit’s *Newman* decision, see our [previous client memorandum](#).

evidence that Newman and Chiasson knew that they were trading on information from insiders or knew that the insiders received a benefit in exchange for their disclosures.

On January 23, 2015, the Government petitioned the Second Circuit *Newman* panel to rehear the case, and alternatively petitioned the Second Circuit to rehear the appeal *en banc*, arguing that *Newman* incorrectly “redefines a critical element of insider trading liability” by “constrict[ing]” the definition of personal benefit. On April 3, 2015, the Second Circuit denied the petition.

The Department of Justice’s Petition for a Writ of Certiorari

On July 30, 2015, the Department of Justice petitioned the United States Supreme Court for a writ of certiorari to review the *Newman* decision. As with the Government’s petition for rehearing and rehearing *en banc*, the [certiorari petition](#) focuses on the Second Circuit’s redefinition of what constitutes a personal benefit sufficient to sustain an insider trading conviction. The Department of Justice does not contest that the Government must prove that a tippee knows of an insider’s receipt of a personal benefit to establish insider trading.

In its petition, the Department of Justice makes three arguments for why Supreme Court review is warranted. First, the Government argues that the Second Circuit’s understanding of “personal benefit” conflicts with and “erroneously departed” from the Supreme Court’s decision in *Dirks v. SEC*, 463 U.S. 646 (1983). *Dirks*, the Department of Justice contends, expressly permitted a personal benefit to be proven when a corporate insider makes a “gift” to a trading relative or friend, without requiring that the insider expect to receive any valuables or money in return and without requiring that the relationship between the insider and tippee be “meaningfully close.” Second, the Government claims that *Newman* conflicts with the decisions of two other courts of appeals.² In *Salman*, the Ninth Circuit expressly disagreed with *Newman*’s interpretation of the personal benefit requirement and stated that *Newman* departed from the Supreme Court’s decision in *Dirks*. The Government also contends that the Seventh Circuit “adhere[d]” to the personal benefit standard under *Dirks* in its *Maio* decision. Third, the Department of Justice argues that the *Newman* decision “frustrates key purposes of the securities laws” and “blurs the lines between legitimate and prohibited activity.” To justify its request for Supreme Court review, the Government claims that the Court’s “[d]elay in doing so will result in continuing and serious harm” to the securities markets.

Likelihood of Supreme Court Review

Newman and Chiasson may file an opposition to the Government’s petition for a writ of certiorari explaining why Supreme Court review is not warranted here, and the Government will have an opportunity to reply. Following conference, the Justices will decide whether to grant the Government’s petition and hear the case. Although the Supreme Court grants review over an exceedingly small number of cases, the apparent split in the lower courts over the proper definition of “personal benefit” in insider trading law makes Supreme Court review of the *Newman* decision more likely.

² *United States v. Salman*, 2015 WL 4068903 (9th Cir. July 6, 2015); *SEC v. Maio*, 51 F.3d 623 (7th Cir. 1995).

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