

U.S. Supreme Court Upholds Insider Trading Conviction Based on Tips from Family Member

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On December 6, 2016, the U.S. Supreme Court issued its first decision addressing the scope of insider trading liability in nearly 20 years. The high court's heavily-anticipated decision in *Salman v. United States of America*¹ arose from petitioner Bassam Yacoub Salman's ("Salman") challenge of his 2014 conviction for insider trading on tips from his future brother-in-law on the grounds that the prosecutors had failed to present sufficient evidence under the standard used by the U.S. Court of Appeals for the Second Circuit (the "Second Circuit") in *United States v. Newman*,² which was widely considered to have raised the bar for insider trading prosecutions. While the Supreme Court upheld Salman's insider trading conviction in an 8-opinion authored by Justice Samuel Alito based on the existence of a family relationship, the Supreme Court's narrow holding continues to leave open questions regarding what constitutes a sufficient "personal benefit" involving other types of relationships or more remote tippee situations.

The government had charged Salman with insider trading and conspiracy arising out of an alleged scheme to trade on inside information originating with his future brother-in-law, Maher Kara, a former analyst in Citibank's healthcare investment banking group, and Maher's brother, Michael Kara. At trial, the government presented evidence that Salman had traded using inside information he had received from Michael Kara, but which he knew had been originally disclosed by his future brother-in-law, Maher Kara. The government also presented evidence at trial that Salman was aware of the Kara brothers' "close fraternal relationship."³ A jury found Salman guilty on all counts, and Salman appealed to the U.S. Court of Appeals for the Ninth Circuit (the "Ninth Circuit").

During the pendency of Salman's Ninth Circuit appeal, the Second Circuit issued its decision in *Newman*, which vacated the convictions of two so-called "downstream" or remote tippees on the grounds that the government had failed to present sufficient evidence that: (i) the tippees knew the information received had been disclosed in exchange for a "personal benefit" and in breach of a fiduciary duty and (ii) the personal benefit comprised something of a "pecuniary or similarly valuable nature."⁴ At Salman's request, the Ninth Circuit panel allowed the parties to submit supplemental briefs to address *Newman*. Nonetheless, on July 6, 2015, the Ninth Circuit affirmed Salman's conviction, rejecting *Newman* and expressly relying on the Supreme Court's 1983 decision in *Dirks v. SEC*.⁵

The resulting circuit split—and Salman's subsequent petition—presented the Supreme Court with the

opportunity to address whether the "personal benefit" to the insider, which the Supreme Court deemed necessary to establish insider trading under *Dirks*, requires proof of "an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature," as the Second Circuit held in *Newman*, or whether it is enough that the insider and the tippee shared a close family relationship, as the Ninth Circuit held in affirming Salman's conviction.⁶

In its unanimous decision, the Supreme Court affirmed the Ninth Circuit's decision upholding Salman's conviction. The Supreme Court characterized the issue presented before it as a narrow one that was "easily resolve[d]" by the long-standing rule espoused in *Dirks* that an insider effectively receives the required personal benefit when disclosure of the inside information is made as a gift to a "trading relative or friend."⁷ The Supreme Court explained that, under these circumstances, "the tipper benefits personally because giving a gift of trading information is the same thing as trading by the tipper followed by a gift of the proceeds."⁸ Because *Dirks* clearly prohibits the latter type of gift, the Supreme Court reasoned that the insider in *Salman*, Maher Kara, should be precluded from "effectively achiev[ing] the same result" by disclosing the information to his brother and to Salman and by then allowing them to trade on it.⁹ According to the Supreme Court, Maher Kara's disclosure of confidential information was a breach of his duty of trust and confidence to his employer and its clients—a duty Salman both acquired and breached by trading on the information despite having knowledge that it was improperly disclosed.¹⁰

The *Salman* case was viewed by many as an opportunity for the Supreme Court to elaborate on the elements of an insider trading violation, particularly in the context of a tipper and downstream tippee, and to clarify an area of the law that had only become more unsettled in the wake of *Newman*. In reality, however, the Supreme Court construed the issue presented very narrowly and expressly limited its holding to the context of a gift of confidential information to a trading relative or friend, drawing on *Dirks* and rejecting *Newman*'s additional requirement of proof of pecuniary gain to the tipper in this specific context. Nonetheless, the *Salman* decision may embolden prosecutors and regulators to investigate and prosecute similar cases, including those in which insiders tip downstream and/or to family member tippees in exchange for purely reputational or other non-pecuniary personal benefits.

¹ *Salman v. United States*, 580 U.S. ____ (2016).

² 773 F.3d 438 (2d Cir. 2014), *cert. denied*, 136 S. Ct. 242 (2015).

³ *U.S. v. Salman*, 792 F.3d 1087, 1090 (9th Cir. 2015).

⁴ *Newman*, 773 F.3d at 455.

⁵ 463 U.S. 646 (1983).

⁶ *Salman v. United States*, 136 S. Ct. 899 (2016).

⁷ *Salman*, 580 U.S. ___, Op. at 10. Notably, the *Salman* decision expressly overturned *Newman* only to the extent its holding can be read to require the tipper to receive "something of a 'pecuniary or similarly valuable nature' in exchange for a gift to family or friends." *Newman* appears to remain good law on other points, including the requirement that a tippee have actual knowledge that the insider disclosed confidential information in exchange for a personal benefit.

⁸ *Id.*

⁹ *Id.* at 9.

¹⁰ *Id.* at 10.