THE NATIONAL LAW REVIEW

U.S. Supreme Court Confirms that a Corporate Insider Receives a "Personal Benefit" by Providing Confidential Information to a Trading Relative or Friend, Affirming Conviction for Insider Trading

Article By Jonathan D. Moss
John P. Stigi III
Sheppard, Mullin, Richter & Hampton LLP
Corporate & Securities Law Blog

Criminal Law / Business Crimes
Litigation / Trial Practice
All Federal

Friday, December 9, 2016

In *Salman v. United States*, No. 15-628, 580 U.S. ___, 2016 WL 7078448 (2016), the United States Supreme Court (Alito, J.) unanimously affirmed the insider trading conviction of petitioner Bassam Salman on the ground that Mr. Salman's brother-in-law had breached his fiduciary duty by making a gift of confidential information to a "trading relative or friend." In doing so, the Supreme Court adhered to its prior ruling in *Dirks v. SEC*, 463 U.S. 646 (1983), and rejected a more lenient application of insider trading liability that the United States Court of Appeals for the Second Circuit had adopted in *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014).

Salman's brother-in-law, Maher Kara, was an investment banker who dealt with highly confidential information about mergers and acquisitions involving his firm's clients. Maher Kara disclosed insider information regarding pending deals to his older brother, Michael Kara. In turn, Michael Kara, without his younger brother's knowledge, fed the information to others, including Salman, who was Michael's friend and Maher's brother-in-law. By the time authorities caught on, Salman had made over $1.5 million in profits trading on this inside information.

Salman was indicted on one count of conspiracy to commit securities fraud and four counts of securities fraud. Facing charges of their own, Maher and Michael each pleaded guilty and testified against Salman at his trial. After trial in the United States District Court for the Northern District of California, Salman was convicted on all accounts and sentenced to 36 months of imprisonment. He appealed to the United States Court of Appeals for the Ninth Circuit. While Salman's appeal was pending, the Second Circuit issued the opinion *Newman*, in which it reversed the insider trading conviction of two portfolio managers, concluding that those defendants were "several steps removed from the corporate insiders" and there was an absence of proof of a meaningfully close relationship between the alleged "tipper" and the "tippees." Pointing to *Newman*, Salman argued that his conviction should be reversed on similar grounds. The Ninth Circuit disagreed and affirmed Salman's conviction, reasoning that the case was governed by the holding in *Dirks* that a tipper of inside information benefits personally by making a gift of such information to a trading relative or friend.

At the Supreme Court, Salman argued that an insider's "gift of confidential information to a trading relative or friend," *Dirks*, 463 U.S. at 664, is not enough to establish securities fraud based upon insider trading. Rather, Salman argued that a tipper does not personally benefit unless the tipper's goal in disclosing inside information is to obtain money, property, or something of tangible value. The government disagreed, arguing that a gift of confidential information to *anyone*, not just a "trading relative or friend," is enough to prove securities fraud. Under the government's view, a tipper personally benefits *whenever* the tipper discloses confidential trading information *for a non-corporate purpose*.

Ultimately, the Supreme Court adhered to *Dirks*, which the Court held "easily resolves the narrow issue presented here." Citing *Dirks*, the Court recognized that "[t]he elements of fiduciary duty and exploitation of nonpublic information . . . exist when an insider makes a gift of confidential information to a trading relative or friend." Recognizing that Maher, the "tipper," provided insider information to a close relative, his brother Michael, the “tippee,” the Supreme Court held that the rule previously set forth in *Dirks* was “sufficient to resolve the case at hand.” The Supreme Court went on to distinguish *Newman*, stating that “[t]o the extent the Second Circuit held that the tipper must also receive something of a ‘pecuniary or similarly valuable nature’ in exchange for a gift to family or friends . . . we agree with the Ninth Circuit that the requirement is inconsistent with *Dirks*.”

In sum, the Supreme Court confirmed that where a tipper provides inside information to a trading relative or friend, the tipper benefits personally because giving a gift of trading information is no different than trading by the tipper followed by a gift of the cash proceeds from the trade to the relative or friend. The Court’s decision marks a victory for the government and bolsters prosecution of corporate insiders for insider trading.