No. 15-628

IN THE

Supreme Court of the United States

BASSAM YACOUB SALMAN,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF *AMICUS CURIAE* SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION IN SUPPORT OF NEITHER PARTY

A. ROBERT PIETRZAK
JOSEPH MCLAUGHLIN
DANIEL A. MCLAUGHLIN
SIDLEY AUSTIN LLP
787 Seventh Avenue
New York, N.Y. 10019
(212) 839-5300

CARTER G. PHILLIPS*
KWAKU A. AKOWUAH
REBECCA S. LEVENSON
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, D.C. 20005
(202) 736-8000
cphillips@sidley.com

Counsel for Amicus Curiae

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* Counsel of Record

QUESTION PRESENTED

Whether an insider trading proceeding brought under the "personal benefit" rule established by *Dirks* v. *SEC*, 463 U.S. 646 (1983), requires proof, based on objective facts and circumstances, that the tipper obtained, directly or indirectly, something of a "pecuniary or similarly valuable nature," consistent with the holding of *United States* v. *Newman*, 773 F.3d 438 (2d Cir. 2014), *cert. denied*, 136 S. Ct. 242 (2015), and if so, whether a case alleging an unlawful tip to a family member must be based on similar proof.

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INTEREST OF *AMICUS CURIAE*[1]

The Securities Industry and Financial Markets Association ("SIFMA") is the voice of the U.S. securities industry, representing broker-dealers, banks and asset managers. Along with their nearly 900,000 employees, SIFMA's members facilitate access to the capital markets; they have raised over $2.4 trillion for U.S. businesses and municipalities; serve clients with over $16 trillion in assets; and manage more than $62 trillion in assets for individual and institutional clients, including mutual funds and retirement plans. SIFMA has offices in New York and Washington, D.C., and is the U.S. regional member of the Global Financial Markets Association (GFMA). Further information about SIFMA can be obtained at http://www.sifma.org.

SIFMA believes that strong and clear rules against insider trading contribute to the efficiency and fairness of the U.S. securities markets. Its members take seriously their obligation to comply with the insider trading laws, and devote significant effort to educating their employees about these laws and supervising their activities. Further, many have adopted company policies that restrict trading in ways that go beyond the requirements of law.

SIFMA also has a strong interest in clarity and predictability in the law. SIFMA members employ thousands of analysts, asset managers, traders, advisors and others whose daily duties involve

[1] Pursuant to Rule 37.6, *amicus* affirm that no counsel for any party authored this brief in whole or in part, and no party or its counsel made a monetary contribution intended to fund the preparation or submission of this brief. Counsel for petitioner and respondent have each consented in writing to the filing of this *amicus* brief.

seeking to advance their own—and ultimately, the market's—grasp of information about public companies. Vague or unpredictable rules about what information may form the basis of trading decisions therefore create undue compliance burdens and legal risks for SIFMA's members and their employees.

SUMMARY OF ARGUMENT

This Court has long recognized that market analysts, investment managers, traders, and other market professionals play a vital informational role in the operation of the securities markets. Analysts and their counterparts are employed by a wide range of financial firms, including investment banks, broker-dealers, mutual funds, and insurance companies. But they broadly share a common mission: to develop new insights about the companies they follow and the valuation of securities issued by those companies.

The Court's path-marking decision in *Dirks* v. *SEC*, 463 U.S. 646 (1983), properly recognized the importance of this function to the "preservation of a healthy market." As the Court explained, "[i]t is commonplace for analysts to ferret out and analyze information," including "by meeting with and questioning corporate officers and others who are insiders" at the companies. *Id* at 658. Information obtained in this way "normally may be the basis for judgments as to the market worth of a corporation's securities," even if that information has not yet been widely disseminated by the company. *Id.* at 659. And "market efficiency in pricing is significantly enhanced by [analysts'] initiatives to ferret out and analyze information, and thus the analyst's work redounds to the benefit of all investors." *Id.* at 658 n.17.

Dirks accordingly rejected the SEC's request for a broad federal rule prohibiting all trading on material non-public information that originated with corporate insiders. Instead, drawing on traditional fiduciary principles that bar insiders from "personally using undisclosed corporate information to their advantage" or from "giv[ing] such information to an outsider for the same improper purpose of exploiting the information for their personal gain," *Dirks* held that the recipient of such information—a "tippee"—likewise may not knowingly exploit an insider's decision to disclose company information for the insider's "personal gain." *Id.* at 659-60.

Dirks cautioned as well that insider trading, so defined, may also occur when "an insider makes a gift of confidential information to a trading relative or friend." *Id.* at 664. Yet, likely because *Dirks* did not involve any such "gift," the Court did not provide detailed guidance as to how to determine whether such a disclosure may give rise to a valid inference that an insider *personally* benefited from the trading profits of a family member or friend.

Recent developments demonstrate the need for further instruction on this issue. The criminal prosecution in *United States* v. *Newman*, 773 F.3d 438 (2d Cir. 2014), *cert. denied*, 136 S. Ct. 242 (2015), is a case in point. There, the government contended that the requisite "personal benefit" to the tipper could be validly inferred from casual social connections that the tipper and initial tippee shared, such as attendance at the same business school or church, or at the same social gatherings. When the Second Circuit reversed, holding that only "meaningfully close personal relationships" can support a "personal benefit" prosecution, *id.* at 452, the government objected in the strongest terms, arguing that "an insider need not be specially attached to his friends and relations in order to decide for his own personal reasons to confer on them a gift of inside information." Petition for Certiorari at 20, *United States* v. *Newman*, No. 15-137 (July 2015).

The government's broad understanding of what constitutes a "gift" actionable under *Dirks*, if adopted, would create significant uncertainty for SIFMA's members and their employees, who receive vast quantities of information about companies from many sources, some known, some unknown, some of uncertain reliability. In addition to companies' SEC filings, press releases and other formal communications, these sources can include the financial press, presentations at investor conferences, blogs, chat rooms, unsolicited tips, rumors, informal analyst networks or social-media platforms like Facebook and Twitter. To the extent that analysts and other SIFMA member employees interact directly with employees of public companies, such interactions over time can take on some of the characteristics of a social or personal relationship. But contrary to the government's position, neither criminal nor civil insider trading liability should turn on whether two people may be described as friends in a casual sense. Any such rule would be unworkable because, as ordinary experience shows, business and personal relationships are constantly in flux, and there is no clear dividing line between casual friendship and simple acquaintance. Legal liability should not turn on that inherently uncertain distinction.

SIFMA respectfully submits, therefore, that insider trading liability should not turn solely on notions of friendship or family relationship alone, but should instead focus on proof that the tipper obtained, directly or indirectly, something of a "pecuniary or similarly valuable nature," consistent with the Second Circuit's conclusion in *Newman*, 773 F.3d at 452. That test would preserve consistency with the core rule announced in *Dirks*: insider trading liability for a tippee must rest on evidence of "objective facts and circumstances" that would support a reasonable inference that the tippee's trading profits are, in practical effect, the tipper's own. *Dirks*, 463 U.S. at 664.

ARGUMENT

The decision below appears at points to suggest that in criminal insider-trading cases, the critical "element of breach of fiduciary duty" invariably "is met where an 'insider makes a gift of confidential information to a trading relative or friend,'" even if the ties that bind the two are weak or casual. Pet. App. 16. So read, the decision in *Salman* stands in considerable tension with the Second Circuit's decision in *Newman*, which held that "the mere fact of a friendship, particularly of a casual or social nature," is not by itself sufficient to establish liability. *Newman*, 773 F.3d at 452.

To be sure, the *Salman* and *Newman* cases present quite different facts. *Salman* involves trading tips exchanged among family members, whereas *Newman* presented questions about the scope of tipping liability where business relationships were alleged to intersect with elements of social relationships. Regardless, the Court's decision here on what constitutes a "personal benefit" under *Dirks* will likely influence how courts view cases that present factual circumstances more akin to *Newman*, and thus far more directly implicate SIFMA's core concern of ensuring that financial market professionals are governed by workable and predictable rules that provide clear guidance about whether they may act on information that they receive in the ordinary course of their business.

Thus, while SIFMA does not take a position on whether the conviction in this case should be sustained, SIFMA does urge the Court to reaffirm that the rule adopted in *Dirks* to distinguish between lawful and unlawful market conduct does not turn on the vagaries of whether and when a business relationship has developed into acquaintance and whether and when acquaintance has developed into friendship. In tippee liability cases, a court's inquiry should instead look to the character of the exchange, and to whether the insider sought ultimately to extract pecuniary value in exchange for the disclosure.

I. FINANCIAL INSTITUTIONS NEED INSIDER TRADING RULES THAT ARE CLEAR AND PREDICTABLE.

SIFMA begins from a premise that should be uncontroversial: The law of insider trading should be structured in a way that allows analysts and other financial market professionals to determine, quickly and with confidence, whether any information in their possession is off-limits to their research and trading activities. This is a critical concern for SIFMA because SIFMA's members distill vast quantities of information into ratings, recommendations and trading decisions, and process huge numbers of trades in connection with managing $16 trillion in broker-dealer assets and $34 trillion of investment advisor assets. See Sec. Indus. & Fin. Mkts. Ass'n, *2015 Year in Review: Invested in America* 7 (2016), http://www.sifma.org/issues/item.aspx?id=8589958792.

SIFMA members take seriously their legal obligations, including the need to prevent violations of the insider trading laws. Section 15(g), 15 U.S.C. § 78o(g), of the Securities Exchange Act of 1934 requires broker-dealers to maintain policies and procedures reasonably designed to prevent the illegal misuse of material nonpublic information by the firm and its employees, and more broadly, one industry survey found that securities firms collectively spent more than $23 billion on compliance activities in a single year—a figure that accounted for 13.1% of their net revenue.[2] SIFMA members also adopt policies that enhance their ability to oversee trading compliance, such as by requiring employees to trade only through in-house accounts and prohibiting employees from trading in certain securities during specified periods.

These compliance efforts—and others tailored to the varying needs of SIFMA's diverse membership—can best succeed when firms and their employees have clear guidance about the legal rules governing trades on the basis of material non-public information. If the law sets clear standards about the kinds of transactions and other activities that are prohibited, it will be easier and less costly for securities firms to design and implement appropriate policies, and easier for employees to conform their conduct to those requirements. In contrast, where guidance of this kind is lacking, "neither corporate insiders nor analysts can be sure when the line is crossed." *Dirks*, 463 U.S. at 659 n.17, and serious due process concerns are raised by the absence of "fair

[2] *See* Sec. Indus. Ass'n, *Survey Report, The Costs of Compliance in the U.S. Securities Industry* 5 (Feb. 2006), http://www.sifma.org/uploadedfiles/research/surveys/costofcompliancesurveyreport(1).pdf?n=87212

notice of what is prohibited." *FCC* v. *Fox Television Stations, Inc.*, 132 S. Ct. 2307, 2317 (2012) (quoting *United States* v. *Williams*, 553 U.S. 285, 304 (2008)); see also *id.* (noting due process roots of the rule that "regulated parties should know what is required of them so they may act accordingly" (citing *Grayned* v. *City of Rockford*, 408 U.S. 104, 108-09 (1972))).

Clear guidance is particularly warranted because SIFMA's members and employees frequently learn information through communications with company officers and employees. This Court went to considerable lengths in *Dirks* to acknowledge the general legitimacy of informational exchanges between professionals, emphasizing that information obtained in this way, even if non-public, "normally may be the basis for judgments as to the market worth of a corporation's securities." See *Dirks*, 463 U.S. at 659. Similarly, testimony adduced at trial in *Newman* showed that "analysts routinely solicited information from companies in order to check assumptions in their models in advance of earnings announcements" and that "investor relations departments routinely assisted analysts with developing their models." 773 F.3d at 454.

With these kind of company-analyst exchanges firmly in mind, *Dirks* accordingly aimed to establish a clear and consistent general framework for insider trading cases involving tippers and tippees. The Court rightly emphasized that it was "essential" to have "a guiding principle for those whose daily activities must be limited and instructed by the S.E.C.'s inside-trading rules," *Dirks*, 463 U.S. at 664, so as to avoid chilling their ability to seek out and act upon information in a way that improves the efficiency of financial markets in valuing companies.

That core concern has echoed across this Court's securities law decisions, which frequently have emphasized the importance of crafting liability rules that are characterized by "certainty and predictability." *Cent. Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 188 (1994) (quoting *Pinter* v. *Dahl*, 486 U.S. 622, 652 (1988)); see also *Pinter*, 486 U.S. at 654 n.29 (if a "test produces unpredictable results, it risks over-deterring" lawful securities market activities). Absent clear and predictable liability rules, market professionals would be exposed to enforcement decisions that are "'made on an ad hoc basis, offering little predictive value' to those who provide services to participants in the securities business." *Cent. Bank*, 511 U.S. at 188. That sort of "shifting and highly fact-oriented disposition" has not been viewed as a "satisfactory basis for a rule of liability imposed on the conduct of business transactions." *Id.* Indeed, it would be particularly inappropriate for criminal insider trading prosecutions to rest on such a foundation for, as this Court repeatedly has stated, the "construction of a criminal statute must be guided by the need for fair warning." *Crandon* v. *United States*, 494 U.S. 152, 160 (1990); see also, *e.g.*, *Ratzlaf* v. *United States*, 510 U.S. 135, 148-49 (1994).

That traditional lenity principle should operate with special force here, where the judiciary has developed a common-law jurisprudence of "tipping" liability without any express direction from the legislature. See *Dirks*, 463 U.S. at 653-55 (describing common-law development of insider trading doctrine). As this Court has previously cautioned, judicially-created liability rules should not be expanded beyond their existing contours without Congressional authorization, see, *e.g.*, *United States*

v. *Skilling*, 561 U.S. 358, 409-11 (2010), consistent with the principle that "legislatures and not courts should define criminal activity." See *United States* v. *Bass*, 404 U.S. 336, 348 (1971); see also *United States* v. *Wiltberger*, 18 U.S. (5 Wheat.) 76, 95 (1820).

If the markets are to operate with optimal efficiency, it is critical that the analyst (and any compliance officer asked to assist) be able to quickly and reliably determine whether trading and recommendations are permitted or prohibited in the circumstances presented. But that can occur only if the insider trading rules are themselves clear and predictable.

II. RECENT ENFORCEMENT ACTIONS UNDER "PERSONAL BENEFIT" THEORIES HAVE CONTRIBUTED TO INCREASING VAGUENESS AND LACK OF CLARITY ABOUT THE SCOPE OF THE INSIDER TRADING PROHIBITION.

The record of enforcement under *Dirks* well illustrates the need for additional clarification about the meaning and application of the "personal benefit" test. Both the SEC and criminal prosecutors frequently have resorted to "doctrinal novelty," *Newman*, 773 F.3d at 448, to bypass any obligation to prove a *quid pro quo*, *i.e.*, that the tipper received something of identifiable value for the information provided. They instead allege that the tips amounted to a "gift" of information to a casual friend or business associate. In some of these cases, the alleged benefit to the tipper was as ephemeral as the supposed enhancement of the tipper's "reputation," or, more fleeting still, the inflation of the tipper's "ego." In others, courts have declared that the fact of disclosure alone is sufficient to prove a "personal benefit"—a clearly erroneous conclusion that strips the "personal benefit" requirement of all meaning. The practical result has been unpredictability and uneven application of the insider trading laws, as courts have grappled with how to apply a watered-down "personal benefit" standard that is supposed to provide some "guiding principle," *Dirks*, 463 U.S. at 664, and yet in the view of some courts can be satisfied in a variety of *sui generis* ways.

These practical concerns are compounded by the transformational changes in information technology that have unfolded in recent years. Today, market professionals may cull information from a wide variety of sources, including social media and other platforms that in various ways can conceal the origins of information, even while multiplying the potential paths of travel across informal networks. The oft-observed result is that it is easier and cheaper than ever for individuals who have a limited personal connection to exchange information on any subject, and without ever meeting in person. For example, a company insider may post information about the company on Twitter; the analyst who sees the tweet may not know what relationship the speaker has to the company; whether the officer or employee is authorized to release the information; or the number of other people who have seen the information.[3]

[3] The SEC's Regulation FD, 17 C.F.R. § 243.100 (2011), was adopted to limit the range of selective disclosures that corporate insiders may make, but the regulation has significant limitations. It does not cover all company insiders and is sometimes misunderstood or misapplied by those who are covered. Thus, as the evidence described in *Newman* well illustrates, *see* 773 F.3d at 454-55, Regulation FD has not stemmed all disclosures of potentially material nonpublic information, nor has it resolved all ambiguity about the permissible use of such information by those who receive it—

An analyst who turns to the case law for guidance about how to handle the avalanche of available information will find little that usefully identifies the material that falls outside the general rule stated in *Dirks*, *i.e.*, that information obtained from companies through professional exchanges "normally may be the basis for judgments as to the market worth of a corporation's securities," *id.* at 659.

Some of the cases simply cannot be reconciled with *Dirks*, insofar as they suggest that an allegation that an insider "disclosed material non-public information," standing "alone," is "enough to allow the Court to find an adequate allegation as to the personal benefit element as well." *SEC* v. *Blackwell*, 291 F. Supp. 2d 673, 692 (S.D. Ohio 2003); see also *SEC* v. *Blackman*, No. 3:99-1072, 2000 WL 868770, at *9 (M.D. Tenn. May 26, 2000) ("[T]he mere fact of [the tipper's] disclosure of this information sufficiently alleges a gift by him to the other defendants so as to satisfy the personal benefit requirement of *Dirks*.").

Other cases unhelpfully tell the analyst that "[t]he showing needed to prove an intent to benefit is not extensive," *SEC* v. *Yun*, 327 F.3d 1263, 1280 (11th Cir. 2003), or, to essentially the same effect, suggest that a damning "personal benefit" inference may be drawn from behavior that would be viewed as benign in virtually any other context. For example, in one controversial case, the SEC settled enforcement charges with a CEO who allegedly corrected estimates previously furnished to analysts in an effort to avoid injury to his professional reputation and his "continued earnings power." See *SEC* v. *Stevens*, SEC

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including ambiguities that may arise because of conflicting recollections about whether the company insider asked the recipient to hold the information in confidence.

Litigation Release No. 12813, 1991 WL 296537, at *1 (Mar. 19, 1991). A leading commentator described this charge as "trivializ[ing] *Dirks*." John C. Coffee, Jr., *The SEC and the Securities Analyst*, N. Y. Law J., May 30, 1991, at 5. And unfortunately, there have been many subsequent examples of similar enforcement actions. See, *e.g.*, *SEC* v. *Sargent*, 229 F.3d 68, 77 (1st Cir. 2000) (tipper often went to tippee for help with local chamber of commerce matters and may have been motivated to maintain a "useful networking contact"); *Yun*, 327 F.3d at 1280-81 ("personal benefit" could be inferred from "friendly" and collaborative relationship between co-workers; jury could conclude that the tipper "expected to benefit from her tip . . . by maintaining a good relationship between a friend and frequent partner in real estate deals"); *SEC* v. *Andrade*, C.A. No. 15-231 S, 2016 WL 199423, at *4 (D.R.I. Jan. 15, 2016) ("personal benefit" inferred from allegation that tipper "personally went with one of his property service vendors to [tippee's] home to help resolve a septic issue for" the tippee); *SEC* v. *McGinnis*, No. 5:14-cv-6, 2015 WL 5643186, at *19 (D. Vt. Sept. 23, 2015) (exchange of family gifts on "customary gift-giving occasions" relevant to benefit); *SEC* v. *Downe*, 969 F. Supp. 149, 156 (S.D.N.Y. 1997) ("personal benefit" inferred from tipper's testimony that he had been motivated by "ego" and personal "gratification"), *aff'd sub nom.* *SEC* v. *Warde*, 151 F.3d 42, 48-49 (2d Cir. 1998).[4]

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[4] A common jury instruction allows a benefit to be found from "maintaining a useful networking contact, improving [the tipper's] reputation, obtaining future financial or employment benefits, or just maintaining or furthering a friendship." *United States* v. *Riley*, ___ F. App'x ___, 2016 WL 158464 at *3 n.3 (2d Cir. Jan. 24, 2016) (unpublished). *Accord United States* v. *Whitman*, 904 F. Supp. 2d 363, 371 n.7 (S.D.N.Y. 2012).

The SEC and criminal prosecutors have not always been successful in persuading courts that an alleged friendship is sufficient to support an insider trading case, but even the defendants who ultimately prevailed have been subjected to extensive and expensive litigation. For example, in *SEC* v. *Anton*, the court rejected the SEC's contention that the alleged tipper, the Chairman of the Board of Directors of a company, had received a personal benefit from providing information to a former executive at the company. No. 06-2274, 2009 WL 1109324, at *9 (E.D. Pa. Apr. 23, 2009). The SEC asserted that the two were "friends" because they had known each other for thirty-five years and that the Chairman had once before invited the executive to his house for dinner, but the court determined that they were "not friends" and therefore, the Chairman was not liable under *Dirks*. *Id.* at *1 n.3, *9. See also *SEC* v. *Maxwell*, 341 F. Supp. 2d 941, 948 (S.D. Ohio 2004) ("Given the parties' relative stations in life, any reputational benefit to [a senior corporate executive] in the eyes of his barber is extremely unlikely to have translated into any meaningful future advantage."); *Newman*, 773 F.3d at 752 (shared alumni and church memberships did not confer a "benefit" because conviction requires "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").

These published decisions—and the many enforcement actions that are resolved by settlement or plea without any extended judicial analysis[5] or by admini-

[5] *Cf. Lafler* v. *Cooper*, 132 S. Ct. 1376, 1388 (2012) (observing that "criminal justice today is for the most part a system of pleas, not a system of trials").

strative adjudication[6]—are a natural outgrowth of liability theories that do little to illuminate what separates lawful from unlawful uses of material nonpublic information, and indeed suggest the difference is "not extensive," *Yun*, 372 F.3d at 1280, or even nonexistent. See *Blackwell*, 291 F. Supp.2d at 692.

Market professionals need far more guidance than this about how to ensure that their conduct remains aligned with the insider trading laws.

III. THE COURT CAN BEST DERIVE A CLEAR AND WORKABLE INSIDER TRADING RULE FROM THE BREACH OF DUTY FRAMEWORK THAT UNDERPINS *DIRKS*.

A. *Dirks* Grounded Tipping Liability In Established Principles Concerning Breach of Fiduciary Duty And Misappropriation Of Corporate Property.

The Court's decision in this case should build on its precedents holding that Section 10(b) does not impose any "general duty between all participants in market transactions to forgo actions based on material, nonpublic information." *Dirks*, 463 U.S. at 655 (quoting *Chiarella* v. *United States*, 445 U.S. 222, 233 (1980)). "[R]ecipients of inside information do not invariably acquire a duty to disclose or abstain," *id.* at 659, but assume that duty only in circumstances that resemble breaches of fiduciary duty recognized by the common law.

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[6] *See, e.g.*, *Lohmann*, SEC Release No. 34-48092, 2003 WL 21468604, at *4 (S.E.C. June 26, 2003) (finding evidence of a personal benefit where the tipper and tippee were "friendly, if casual, office acquaintances" and the tipper stood to gain "the personal satisfaction of his generosity and the admiration" of a junior colleague).

Two firmly accepted principles underlie that approach. The first is that inside information belongs to the corporation and its shareholders, and not to any individual officer or employee. The second is that because a corporate insider owes fiduciary duties to the company, the insider may not derive "secret profits," *id.* at 654 (quoting *Cady, Roberts & Co.*, 40 S.E.C. 907, 916 n.31 (1961)), by trading on undisclosed information that is "intended to be available only for a corporate purpose." *Id.* at 654. Some early cases treated such trading as fraudulent, see *Cady, Roberts*, 40 S.E.C. at 911 n.13 (citing *Strong* v. *Repide*, 213 U.S. 419 (1909)), and "[a] significant purpose of the Exchange Act was to eliminate the idea that use of inside information for personal advantage was a normal emolument of corporate office." *Dirks*, 463 U.S. at 653 n.10 (quoting *Cady, Roberts*, 40 S.E.C. at 912 n.15).[7]

The prohibition on insider trading by tippees rests on fundamentally the same footing. "[T]ipping thus properly is viewed only as a means of *indirectly* violating" the rule that an insider who possesses material non-public information must either disclose that information or refrain from trading on it. *Dirks*, 463 U.S. at 659, 661 (emphasis added). Put another way, the tippee's liability is "derivative"; it arises only

[7] A corporate outsider who receives material nonpublic information from a company or an insider and trades on the information in violation of a confidentiality undertaking or duty of trust and confidence to the source of the information has likewise been treated as guilty of fraud under the "misappropriation" theory; the conduct is treated as a fraud, carried out by a faithless fiduciary, and aimed at depriving the *source* of the information of its ownership of that information. *See United States* v. *O'Hagan*, 521 U.S. 642, 654-55 (1997) (Section 10(b)); *Carpenter* v. *United States*, 484 U.S. 19, 27 (1987) (mail and wire fraud).

where the tippee can be viewed as "a participant after the fact in the insider's breach of a fiduciary duty." *Id.* at 659, 661 n.20 (quoting *Chiarella*, 445 U.S. at 230 n.12).

This reasoning led the Court to reject the SEC's suggestion "that the antifraud provisions [of the securities laws] require equal information among all traders." *Id.* at 657. The rule, rather, is that "some tippees must assume an insider's duty to the shareholders not because they receive inside information, but rather because it has been made available to them *improperly*." *Id.* at 660.

B. The "Personal Benefit" Test Should Likewise Be Construed In Light Of Traditional Fiduciary Principles.

The "personal benefit" test was founded on this same understanding of the antifraud statutes and, accordingly, should be applied in a manner that similarly focuses on "whether the insider personally will benefit, directly or indirectly, from his disclosure," for "[a]bsent some personal gain, there has been no breach of duty to stockholders. And absent a breach by the insider, there is no derivative breach," and no violation of Section 10(b) by the tippee. See *id.* at 662.

To be sure, *Dirks* stated that a breach occurs not only where "the insider receives a direct or indirect personal benefit from the disclosure, such as a pecuniary gain or a reputational benefit that will translate into future earnings," *id.* at 663, but also "when an insider makes a gift of confidential information to a trading relative or friend." *Id.* at 664. But the Court had no occasion in *Dirks* to apply or define the latter portion of its test, relating to "gifts," that is at issue here.

In a business setting, a finder of fact should not be permitted to impose liability on the theory that a "gift" was made, and liability may follow, simply because a company insider provided material nonpublic information to an analyst or other market professional. That sort of standard would swallow the general rule, recognized in *Dirks*, that financial market professionals generally may work to "ferret out" non-public information, and generally may act on the basis of such information, if it comes into their possession. *Id.* at 658.

Nor should liability be permitted to rest on the fact that an analyst or other market professional has developed casual social ties to the tipper. People seldom interact on a regular basis without developing some degree of acquaintance or familiarity, but that fact alone does not warrant an inference that every disclosure is meant to be a "gift" to the tippee. That approach, too, threatens to swallow the general rule of *Dirks*, and to leave market participants without any meaningful "guiding principle," *id.,* at 664, as to where liability lies. In these situations, *Newman* surely had it right that acquaintance or familiarity or even some degree of "friendship" should not justify an inference that there has been a "gift" absent a relationship that is "meaningfully close" and that "generates an exchange that is objective, consequential and [that] represents at least a potential gain of a pecuniary or similarly valuable nature." 733 F.3d at 452. And under *Dirks*, the closeness of the relationship and the significance of the exchange must be established by "objective criteria." *Dirks*, 463 U.S. at 663.

In the business setting, such criteria could include evidence that shows that "the insider, by giving the information out selectively, is in effect selling the information to its recipient for cash, reciprocal information, or other things of value for himself." *Id.* at 664 (quoting Brudney, *Insiders, Outsiders, and Informational Advantages Under the Federal Securities Laws*, 93 Harv. L. Rev. 322, 348 (1979)). Evidence that the tipper shared the information (or was willing to share the information) with others who provided nothing in "exchange" would tend to undermine the inference of "personal gain." But whatever the specific evidence in the case, the inquiry should at bottom look to the character of the exchange, and whether the insider seeks ultimately to extract pecuniary value for the disclosure.

Though SIFMA does not take a position on the proper application of the *Dirks* standard to the facts of this case, the same core principle should govern in the family setting. Something more than the mere fact of a family relationship should be required, contrary to the SEC's recent suggestion that, for example, "[f]irst cousins have sufficient consanguinity to be meaningfully close as a matter of law." Brief of the SEC at 33 n.13 in *SEC* v. *Holley*, No. 15-3457 (3d Cir. filed Apr. 20, 2016). In fact, many persons who are related by blood or marriage are not aware of each other; many others are estranged or hostile. The evidence establishing liability under the "gift" theory in the family setting might demonstrate a history of reciprocal favors, mutual dependence and shared economic circumstances to the extent that it may fairly be inferred that a benefit nominally realized by a tippee family member accrues to the benefit of the tipper and possibly other family members. On the other hand, it would (as above) contradict such an inference if the tipper had shared the information (or was willing to share the information) with persons who are not family members and provided no other reciprocal benefit.

Making clear that tipping liability cannot rest on relationship status alone would greatly clarify the law of tippee liability, particularly as applied to business settings. For one, it would have the laudable effect of freeing the lower courts from their current focus on matters like whether the tipper and tippee were "friends," as evidenced by ties like whether "two individuals were alumni of the same school or attended the same church," see *Newman*, 773 F.3d at 452. As demonstrated in Part II, *supra*, inquiries like these have produced inconsistent results across cases, in no small measure because there is no federal common law of friendship, and thus no firm guideposts for courts to follow. It would be appropriate instead to make clear that insider trading cases brought under a "gift" theory must operate within the "solid core" of Section 10(b) and Rule 10b-5, cf. *Skilling*, 561 U.S. at 407, and thus must likewise focus on the character of the exchange and rest ultimately on proof that the tipper obtained pecuniary value for the information disclosed.

Second, such a holding would make it much easier for market professionals to know whether their conduct complies with the law. No one should be required to guess at whether the SEC, a prosecutor or a jury would think that the threshold for an actionable friendship is two meals or four, or membership in the same or adjoining college class years. But market professionals can be fairly required to ask and answer a more targeted question: Would the person who provided this information benefit in any pecuniary sense if his or her intended recipient used the information to make a profit? Ties of friendship or blood or marriage might in some circumstances be *relevant* to that more targeted question. But rather than resting liability on the slender reed of a third party's abstract understanding of friendship or family ties, the analysis should turn more concretely on whether the insider is, in one respect or another, lining his own pocket by disclosing the information. What was true at the time of *Dirks* remains true today: "'It is important in this type of case to focus on policing insiders and what they do . . . rather than on policing information *per se* and its possession." *Dirks*, 463 U.S. at 662-63 (quoting *In re Investors Mgmt. Co.*, 44 S.E.C. 633, 648 (1971) (Commissioner Smith, concurring in result)).

Third, a targeted inquiry into the insider's potential for personal benefit would provide additional clarity in cases such as *Newman*, in which the defendant is the remote recipient of information, many conversations removed from the original tip. The defendant might know whether the insider and the first tippee went to college or play golf or sing in a choir together, but in ordinary life no one draws nefarious conclusions from such commonplace ties. Rather than asking whether the ultimate tippee knew innocuous facts like these, courts can come more quickly and decisively to the point by asking whether the trader had sufficient knowledge that the insider would benefit in monetary terms as a result of profits earned by a direct or remote tippee.[8]

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[8] While the standard for knowledge or conscious avoidance is not directly in issue (including the question, long reserved by this Court, of whether recklessness is an adequate basis for Section 10(b) civil liability), the personal benefit requirement is closely connected to the distinct question of the tippee's knowledge of the breach of duty. *See Dirks*, 463 U.S. at 660-61 & n.19. Indeed, the government has recognized in *Newman* and elsewhere that the two issues are intertwined, sometimes

Finally, the approach suggested here would square with Congress's apparent ratification of the basic understanding that insider trading consists of a breach of duty by an insider, as motivated by an opportunity to obtain a personal benefit. Congress specifically addressed insider trading twice in the years immediately following *Dirks*,[9] yet it chose not to disturb the *Dirks* approach at a time when other developed markets were statutorily eliminating the requirement of a breach of duty.[10] See *SEC* v. *Clark*, 915 F.2d 439, 451-53 (9th Cir. 1990) (treating 1984 and 1988 insider trading enactments as Congressional ratification of "misappropriation" theory); see also *Halliburton Co.* v. *Erica P. John Fund, Inc.*, 134 S. Ct. 2398, 2411 (2014) (noting that "[t]he principle

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contending that the tippee's knowledge can be shown simply by the quality of the information disclosed. *See* Petition for Certiorari at 30, *United States* v. *Newman*, No. 15-137; *cf., Yun*, 327 F.3d at 1280. But many of the controversies over the government's methods for proving knowledge are consequences of the ambiguity of the "personal benefit" in the first place. If tipping cases are limited to those in which the benefit is objective and concrete, the government will need to rely on fewer substitutes for proving knowledge (if it can prove it at all), and it will have less reason to ask courts and juries to accept unwarranted inferences; thus, administration of this aspect of tipping cases can be greatly simplified.

[9] *See* Insider Trading Sanctions Act of 1984, Pub. L. No. 98-376, 98 Stat. 1264; Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, 102 Stat. 4677.

[10] For example, not long after *Dirks*, European officials adopted insider trading rules that prohibit recipients of undisclosed corporate information from trading on their special knowledge, regardless of whether the insider has sought to gain from the disclosure. *See* Council Directive Coordinating Regulations on Insider Dealing, Council Directive 89/592, *Coordinating Regulations on Insider Trading*, 1989 O.J. (L 334) 30. Congress has not chosen that path.

of *stare decisis* has special force in respect to statutory interpretation because Congress remains free to alter what we have done"). If the application of the insider trading laws to tippees is to shift away from the *Dirks*-endorsed foundation in principles of fiduciary duty and corporate misappropriation, any such change should be initiated by Congress. The legislature is far better positioned than the courts to weigh the potential virtues and drawbacks of competing insider liability standards and, in adopting any amendments, to provide the clarity that has been absent from enforcement actions predicated on vague and shifting understandings of how friendships are formed and maintained—a subject that is generally foreign to the securities laws, and has no natural place within them.

CONCLUSION

The Court should once again recognize the significant contribution that analysts and other market professionals make to the efficiency of the securities markets, including by "meeting with and questioning corporate officers and others who are insiders," *Dirks*, 463 U.S. 658, and should reaffirm that those who receive company information may act on that information unless they are aware that a tipper disclosed the information in order to obtain a personal benefit of a "pecuniary or similarly valuable nature." *Newman*, 773 F.3d at 452.

Respectfully submitted,

A. ROBERT PIETRZAK
JOSEPH MCLAUGHLIN
DANIEL A. MCLAUGHLIN
SIDLEY AUSTIN LLP
787 Seventh Avenue
New York, N.Y. 10019
(212) 839-5300

CARTER G. PHILLIPS*
KWAKU A. AKOWUAH
REBECCA S. LEVENSON
SIDLEY AUSTIN LLP
1501 K Street, N.W.
Washington, D.C. 20005
(202) 736-8000
cphillips@sidley.com

Counsel for Amicus Curiae

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* Counsel of Record