Salman Rejects Heightened Personal-Benefit Requirement in Insider Trading Prosecutions

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On December 6, 2016, the U.S. Supreme Court in *Salman v. United States* unanimously held that an insider's gift of confidential information to a "trading relative or friend" is sufficient to establish the personal benefit to the tipper that is required for an insider trading prosecution of the tippee. In so doing, the Court rejected the U.S. Court of Appeals for the 2nd Circuit's holding in *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014), to the extent that court held that an insider also must receive something of a pecuniary or similarly valuable nature in exchange for that gift to family and friends.

At trial, Bassam Salman was convicted of conspiracy and insider trading in violation of Section 10(b) of the Securities Exchange Act of 1934. Salman's brother-in-law, Maher Kara, an investment banker with access to confidential nonpublic information regarding corporate transactions, provided that information to his brother Michael, expecting that Michael would trade on it. Michael shared the information with Salman, who also traded on it and thereby earned more than $1.5 million. However, the evidence at trial did not establish that Maher received anything of pecuniary value in exchange for the information.

On appeal to the U.S. Court of Appeals for the 9th Circuit, Salman relied on *Newman* to argue that because Maher (the insider) made a gift of confidential information to a trading relative or friend (Maher's brother Michael) but did not receive a pecuniary benefit in exchange, the evidence failed to establish the personal benefit to the insider required by *Dirks v. SEC*, 463 U.S. 646 (1983). In *Dirks*, the Court held that a tippee is not liable for trading on the basis of material nonpublic information provided by an insider unless the insider "personally will benefit, directly or indirectly, from his disclosure," such that the tippee's trading can be linked to the insider's breach of fiduciary duty. 463 U.S. at 662. Salman argued that, pursuant to *Newman*, a personal benefit cannot be inferred "in the absence 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." 773 F.3d at 452. The 9th Circuit disagreed and upheld Salman's conviction, observing that *Dirks* held that a personal benefit to the insider can be inferred when an insider makes a gift of confidential information to a trading relative or friend. *Salman v. United States*, 792 F.3d 1087 (9th Cir. 2015).

In an opinion authored by Justice Samuel A. Alito Jr., a unanimous Court in *Salman* affirmed, holding that adherence to *Dirks* "easily resolves the narrow issue" presented. Slip op. at 8. The Court explained that the tippee can be liable only if he participates in the breach of the insider's fiduciary duty, a question that turns in large part on whether the insider personally benefitted from the disclosure. The Court further explained that the elements of a breach of duty can be established when the tipper obtains a pecuniary gain or a reputational benefit that translates into personal earnings but also, quoting *Dirks*, "when an insider makes a gift of confidential information to a trading relative or friend." Slip op. at 9.

The Court held that the gift-giving discussion in *Dirks* was dispositive in *Salman*, where Maher (the tipper) gave information to Michael (the tippee) with the expectation that Michael would trade on it, and where Salman also traded on that information, with full knowledge that the information had been disclosed improperly. The Court further stated that to require that the insider also receive something of a pecuniary or similarly valuable nature in exchange for that gift, as the 2nd Circuit required in *Newman*, was not consistent with *Dirks*, abrogating that aspect of the 2nd Circuit's decision. The Court noted that *Salman* did not raise (and the Court therefore did not address) another aspect of the *Newman* decision — namely, that the 2nd Circuit reversed the convictions in that case because the government introduced no evidence that the trading defendants knew that the information they traded on came from insiders or knew that the insiders received a personal benefit in exchange for the tips.

Notably, the Court denied *certiorari* in *Newman* in October 2015 before granting *certiorari* in *Salman* in January 2016. The Court may have viewed *Salman* as the better vehicle for addressing the *Dirks* rule, as the government in *Newman* sought review only on the question of personal benefit to the insider. Pet. for Writ of Cert. at I, *United States v. Newman*, No. 15-137 (Jul. 30, 2015). Had the Court granted *certiorari* in Newman, its holding would not have reversed the 2nd Circuit in light of the remaining issue concerning the tippees' knowledge.

While hailed as a victory for prosecutors and Securities and Exchange Commission officials pursuing insider trading cases, the *Salman* decision is a limited one. It clarifies that where an insider makes a gift of confidential information to a trading relative or friend, within the heartland of the *Dirks* rule, no more is required to establish a personal benefit to the insider. In that specific context, it rejects *Newman*'s additional requirement that the insider receive something of a pecuniary or similarly valuable nature in exchange. However, it leaves for another day more difficult questions including what constitutes a sufficiently close friendship to fall within the *Dirks* rule, what establishes a personal benefit to the insider in cases that fall outside that rule, and the level of knowledge that must be proven with respect to remote tippees who are more removed from the corporate insiders than the defendant in this case.