Insider trading claims survive if close in time

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The 9th U.S. Circuit Court of Appeals held that a plaintiff bringing an insider trading claim under Section 20A of the Securities Exchange Act of 1934 does not need to allege or prove that she sold a security to or purchased a security from the defendant. *In re Silver Lake Group, LLC Sec. Litig*, 108 F.4th 1178 (9th Cir. 2024). Instead, the plaintiff must show that she purchased "the same class" of security "contemporaneously" with the defendant's trading activity, which means that the "transactions" must be "close in time." *Id*. at 1089-90.

Although the 9th Circuit held that Section 20A does not require contractual privity between the parties, it did not address how close in time the parties' trades must be to satisfy Section 20A's contemporaneous trading rule.

The 9th Circuit did not specify how close the plaintiff's trading activity must be to the defendant's to satisfy the rule. However, the emerging consensus among lower courts is that Section 20A's contemporaneous trading rule requires the plaintiff's trades to occur within roughly 24 hours (depending on the circumstances) after the defendant's trades. Moreover, the decision highlights that investors always need to think carefully about whether they possess material, non-public information before trading, even when they are trading in the private market after hours.

The 9th Circuit's decision

Section 20A of the Exchange Act provides that: "Any person who … purchas[es] or sell[s] a security while in possession of material, nonpublic information shall be liable … to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased … or sold … securities of the same class." 15 U.S.C. § 78t-1(a).

In *Silver Lake*, the plaintiffs alleged that the defendants sold stock in a satellite communications company through after-hours trading after learning that the Federal Communications Commission planned to revoke the company's license to use a particular broadcast frequency. The district court dismissed the complaint.

On appeal, the defendants argued that the plaintiffs could not satisfy Section 20A's contemporaneous trading requirement because they purchased stock on the public market, while the defendants sold stock through private, after-hours trading. Arguing that the contemporaneous trading requirement was meant to "weed[] out plaintiffs who could not have possibly traded with the" defendant, defendants argued that because the parties' trades were not made in the same market, there was no possibility that plaintiffs bought stock from the defendants, and, therefore, their trades were not contemporaneous.

The 9th Circuit disagreed. The court held that Section 20A does not require that the parties actually traded with one another, or even that it was possible for the plaintiffs to have purchased their securities from or sold their securities to the defendants. Instead, the court held that, notwithstanding the aim of the rule to serve as a proxy for privity, Section 20A's contemporaneous rule "merely requires that the seller and buyer engaged in transactions close in time, not with each other." Silver Lake, 108 F.4th at 1090.

In so holding, the court resolved an issue that district courts had previously addressed in the class certification context — whether the contemporaneous trading requires privity or the potential for privity, or merely temporal proximity — an issue the 9th Circuit previously declined to address on appeal. *See, e.g., See Turocy v. El Pollo Loco Holdings, Inc.*, No. SA CV 15–1343–DOC (KESx), 2018 WL 3343493, at *17 (C.D. Cal. July 3, 2018).

The court went on to affirm the district court's judgment for the defendants, holding that the plaintiffs failed to sufficiently allege that the defendants traded on material, non-public information.

How close is close enough?

Although the 9th Circuit held that Section 20A does not require contractual privity between the parties, it did not address how close in time the parties' trades must be to satisfy Section 20A's contemporaneous trading rule. While the 9th Circuit has in the past stated that the time period is "not fixed," *Neubronner v. Milken*, 6 F.3d 666, 670 (9th Cir. 1993), it has declined to refine this standard further on previous occasions as well, including, for example, after a Section 20A class of investors was certified in *Turocy v. El Pollo Loco Holdings, Inc*.

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Nevertheless, while not uniform in their rulings, lower courts lean toward a rule that a plaintiff must purchase or sell shares within roughly 24 hours (depending on the circumstances) after the defendant's trading activity to satisfy the contemporaneous trading requirement. Indeed, this appears to be the emerging consensus.

While in *Silver Lake* the 9th Circuit explained, "[t]he word 'contemporaneous' denotes a temporal proximity and means 'existing, occurring, or originating during the same time,'" *Silver Lake*, 108 F.4th at 1089, lower courts have not focused on this plain meaning when considering what length of time is appropriate.

Some courts, without engaging directly in a textual analysis, have concluded that once plaintiff's trades are more than a day or so apart from the defendant's, it becomes difficult, and perhaps impossible, to credibly argue that the trades occurred or originated during the same time. *See, e.g., Buban v. O'Brien*, 1994 WL 324093, at *3 (N.D. Cal. June 22, 1994) (concluding trades three days apart could not be contemporaneous).

But other courts have permitted a longer time gap — five days or even longer — stating that "contemporaneous" means a "reasonable period" or the period during which the defendant possessed undisclosed material information, without tying these conclusions to the definition of the word, "contemporaneous." *See, e.g., In re Oxford Health Plans*, 187 F.R.D 133, 144 (S.D.N.Y. 1999); *In re Am. Bus. Comps. Sec. Litig.*, 1994 WL 848690, at * (S.D.N.Y. Feb. 24, 1994).

Lower courts have also concluded that a 24-hour rule is consistent with the contemporaneous trading rule's purpose, along with the principles of Article III standing. The contemporaneous trading rule is designed to limit Section 20A claims to those plaintiffs who could have plausibly traded with the defendant and been harmed by trading at an unfair information disadvantage. *See, e.g., Brody v. Transitional Hosp. Corp.*, 280 F.3d 1005 (9th Cir. 2002).

Thus, while Section 20A does not impose a contractual privity requirement (which would be difficult or impossible to prove in many cases), it is meant as a "stand-in" for a privity. *Silver Lake*, 108 F.4th at 1190.

Courts have concluded that plaintiffs who make their trades more than about 24 hours after the defendant's trades are not part of the class of investors who could have plausibly traded with the defendant, and, therefore, fall outside of the circle of investors the statute was meant to protect. *See, e.g., In re Countrywide Fin. Corp. Sec. Litig.*, 588 F. Supp. 2d 1132, 1204-05 (C.D. Cal. 2008); *In re Fed. Nat'l Mortg. Ass'n Sec., Derivative, & "ERISA" Litig.*, 503 F. Supp. 2d 25, 47 (D.D.C. 2007); *In re MicroStrategy, Inc. Sec. Litig.*, 115 F. Supp. 2d 620, 663-64 (E.D. Va. 2000).

For similar reasons, lower courts have concluded that permitting plaintiffs who traded more than 24 hours or so after the defendant's trades to bring Section 20A claims might pose Article III standing problems. Plaintiffs bringing federal statutory claims must show that they were "concretely harmed by a defendant's statutory violation." *TransUnion LLC v. Ramirez*, 594 U.S. 413, 427 (2021).

In insider trading cases, the plaintiff's alleged harm is that she traded at a material informational disadvantage to other investors. *Silver Lake*, 108 F.4th at 1189. That harm becomes less concrete and more speculative the farther away the plaintiff's trades are from the defendant's, because as the issuer's stock price changes in response to new information, it becomes harder to tell whether the plaintiff transacted at a price that was less favorable than the defendant. *See MicroStrategy*, 115 F. Supp. 2d at 663-64; *In re AST Research Sec. Litig.*, 887 F. Supp. 231 (C.D. Cal. 1995); *Buban*, 1994 WL 324093, at *3.

By restricting Section 20A claims to plaintiffs who purchased soon after the defendant, it is more likely that the plaintiff and the defendant transacted in the same trading environment, such that the plaintiff was actually harmed by the alleged information asymmetry.

While in *Silver Lake* the 9th Circuit did not articulate a bright-light rule for the timing of the contemporaneous trading rule, the court's definition of "contemporaneous" and its reinforcement of the characterization of the rule as a stand-in for privity, resonates with the emerging consensus that suggests a 24-hour limit.

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