UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, **Plaintiff,** **v.** **DARYL M. PAYTON, and BENJAMIN DURANT, III,** **Defendants.**	**Civil Action No. 14-cv-04644-JSR** **ECF CASE**

PLAINTIFF SECURITIES AND EXCHANGE COMMISSION'S OPPOSITION TO DEFENDANTS' MOTION TO DISMISS

SECURITIES AND EXCHANGE COMMISSION
David L. Axelrod
Catherine E. Pappas
A. Kristina Littman
One Penn Center
1617 JFK Blvd, Suite 520
Philadelphia, PA 19103
(215) 597-3100

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INTRODUCTION

This matter involves unlawful insider trading ahead of International Business Machines Corporation's ("IBM") 2009 acquisition of SPSS Inc. ("SPSS") by two securities industry professionals, defendants Daryl M. Payton and Benjamin Durant, III. As a result of their illegal insider trading, defendants Payton and Durant made ill-gotten gains exceeding $290,000. Am. Compl. ¶ 3.

In late May 2009, Trent Martin, an equities salesman at a registered broker-dealer, learned material, nonpublic information regarding IBM's pending acquisition of SPSS (the "SPSS Acquisition") from his close friend, Michael Dallas, an associate at a New York law firm who worked on the acquisition. Am. Compl. ¶ 2. Martin misappropriated the information about the SPSS Acquisition from Dallas (the "Inside Information"), purchased SPSS securities on the basis of that information, and tipped that information to his friend and roommate, Thomas Conradt. Am. Compl. ¶ 2. Conradt tipped defendants Payton and Durant, who then violated the securities laws by using this information to trade SPSS securities in anticipation of the SPSS Acquisition. Am. Compl. ¶ 2.

Defendants mistakenly contend that this action should be dismissed because the Complaint, as originally filed, fails to state a claim for insider trading in light of *United States v. Newman*, 773 F.3d 438 (2d Cir. 2014).[1] Specifically, defendants claim the Complaint fails to allege: (1) Martin received a benefit for passing the misappropriated information to Conradt; (2) defendants knew Martin received a benefit for passing the misappropriated information to Conradt; and (3) defendants knew or should have known Martin breached a duty to Dallas when

[1] Defendants filed their motion to dismiss on February 23, 2015. Dkt. 29. On March 2, 2015, the Commission filed the Amended Complaint. Dkt. 32.

he tipped Conradt. Additionally, defendant Durant contends that the Complaint's allegations regarding his insider trading are legally infirm.

Defendants' arguments miss the mark. First, the Commission is not required to plead that Martin received a benefit in exchange for breaching his duty to Dallas or defendants' knowledge of such benefit because the Commission brought this case under the misappropriation theory of insider trading, where the breach is inherent in the deceptive conduct involved. Second, even assuming that the pleading requirements under a misappropriation theory are the same as under the classical theory, the allegations in the Amended Complaint satisfy the Supreme Court's decision in *Dirks v. SEC*, 463 U.S. 646 (1983) and even the most unreasonable reading of *Newman*. Third, contrary to defendants' argument, the Commission need only plead facts permitting the inference that defendants knew or should have known that confidential information was obtained and transmitted in violation of a breach of duty of trust or confidence for personal benefit, and the allegations in the Amended Complaint easily satisfy the factors courts evaluate to determine whether this element has been sufficiently pled. Finally, Durant has more than adequate notice of the claims against him because the Amended Complaint eliminates any conceivable ambiguity about the government's theory of Durant's liability.

The defendants' motion should be denied.

STANDARD OF REVIEW

In considering a motion to dismiss under Federal Rule of Civil Procedure 12(b)(6), the court must accept all well-pleaded factual allegations in the complaint as true, and draw all reasonable inferences in favor of the plaintiff. *SEC v. Apuzzo*, 689 F.3d 204, 207 (2d Cir. 2012); *SEC v. Wyly*, 788 F. Supp. 2d 92, 101 (S.D.N.Y. 2011). A motion to dismiss should be granted only if the complaint is unable to articulate "enough facts to state a claim to relief that is

plausible on its face." *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 570 (2007); *see also Ashcroft v. Iqbal*, 556 U.S. 662 (2009). A complaint need not contain detailed factual allegations. If the complaint contains sufficient "factual content" to allow "the court to draw the reasonable inference that the defendant is liable for the misconduct alleged," the plaintiff has met its burden of stating a claim with "facial plausibility." *Iqbal*, 556 U.S. at 678; *see also Wyly*, 788 F. Supp. 2d at 101.

Upon a motion to dismiss the court should not evaluate the merits of the allegations. "A well-pleaded complaint may proceed even if it strikes a savvy judge that actual proof . . . is improbable, and that a recovery is very remote and unlikely." *Twombly*, 550 U.S. at 556 (quotation omitted). *See also Walker v. Schult*, 717 F.3d 119, 124 (2d Cir. 2013) (on motion to dismiss, court should not "assay the weight of the evidence which might be offered in support thereof") (*citing DiFolco v. MSNBC Cable L.L.C.*, 622 F.3d 104, 113 (2d Cir. 2010)); *Elastic Wonder, Inc. v. Posey*, Case No. 13 CV. 5603 (JGK), 2015 WL 273691, at *1 (S.D.N.Y. Jan. 22, 2015) (function of motion to dismiss is not to weigh evidence). For this reason, a motion to dismiss for failure to state a claim is viewed with disfavor and is rarely granted. *Freudenberg v. E*Trade Financial Corp.*, 712 F. Supp. 2d 171, 178-79 (S.D.N.Y. 2010).

Rule 8 of the Federal Rules of Civil Procedure requires "a complaint to make a short, plain statement of a plausible claim for relief, while Rule 9 requires that the circumstances constituting the fraud be stated with particularity. "[Rule 9] is intended to provide defendants with fair notice of the plaintiff's claim, to discourage plaintiffs from making a cavalier decision to accuse a defendant of fraud . . . ." *SEC v. One or more Unknown Traders in Securities of Onyx Pharma., Inc.*, No. 13-CV-4645, 2014 WL 5026153, at *3 (S.D.N.Y. Sept. 29, 2014), *citing ATSI Communications, Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 99 (2d Cir. 2007).

However, Rule 9(b) is "relaxed" in the context of insider trading "because insider tips are typically passed on in secret" and thus it is "impractical to require plaintiffs to allege these details with particularity." *Onyx*, 2014 WL 5026153, at *4. In an insider trading matter, the plaintiff may simply "plead facts that imply the contents and circumstances of an insider tip." *Id*.

ARGUMENT

I. UNDER THE MISAPPROPRIATION THEORY OF INSIDER TRADING THE COMMISSION NEED NOT PROVE MARTIN RECEIVED A PERSONAL BENEFIT, OR THAT DEFENDANTS HAD KNOWLEDGE OF SUCH A PERSONAL BENEFIT.

Defendants mistakenly contend that the Commission has failed to sufficiently plead that Martin received a personal benefit for misappropriating the Inside Information. *See Memorandum of Law in Support of Defendants' Motion to Dismiss* ("*Defs.' Mem.*") at 1. This insider trading matter has been brought under the misappropriation theory of insider trading, where, unlike a case brought under the classical theory, the tipper need not receive a personal benefit in order to breach a duty.

The distinct duties underlying the classical and misappropriation theories give rise to different types of breaches of those duties, such that a personal benefit is required for breach under the classical theory but not required for breach under the misappropriation theory. In a classical theory case, a person breaches a duty owed to the corporate shareholders when he trades on or tips confidential information for a personal, rather than corporate, purpose. *Chiarella v. United States*, 445 U.S. 222, 228 (1980); *Dirks*, 463 U.S. at 653 n.10 (discussing *In the Matter of Cady, Roberts & Co.*, 40 S.E.C. 907, 912 n.15 (1961)). There must be a personal benefit to the insider that distinguishes an insider's proper corporate use of confidential information from an improper personal use of confidential information. *Dirks*, 463 U.S. at 661-62.

In contrast, in a case such as this, brought under the misappropriation theory, a person breaches a duty to the source of the information by stealing that information and using it for the unauthorized purpose of trading or tipping someone else to trade on it. *United States v. O'Hagan*, 521 U.S. 642, 652 (1997); *United States v. Libera*, 989 F.2d 596, 600 (2d Cir. 1993) ("This fraud has been analogized to embezzlement . . . and may simply be thought of as the misuse, by trading, of stolen information."). A misappropriation case requires no showing of a personal benefit to the tipper, because the breach is inherent in the tipper's theft of confidential information. The theft alone, in violation of the source of information's property right to the information, is a breach of the person's duty to the source of the information. *See Libera*, 989 F.2d at 600; *SEC v. Materia*, 745 F.2d 197, 202 (2d Cir. 1984).[2]

Given this distinction between the two theories the Second Circuit has twice strongly suggested that personal benefit is not an element of a misappropriation case.[3] In *Libera*, the Second Circuit listed the elements of tippee liability under the misappropriation theory without including personal benefit. 989 F.2d at 600. *Cf. SEC v. Sargent*, 229 F.3d 68, 77 (1st Cir. 2000) (noting that, in *Libera*, the "Second Circuit strongly implied . . . in dicta [ ] that there was no need to make an affirmative showing of benefit in cases of misappropriation"). Later, in *United States v. Falcone*, the Second Circuit reiterated that standard. 257 F.3d 226, 234 (2d Cir. 2001).

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[2] Contrary to defendants' argument, the Supreme Court has not suggested that the elements of a classical case and misappropriation case are the same. *See Defs.' Mem.* at 5 n.1. In *O'Hagan* the Court stated that the "two theories are complementary, each addressing efforts to capitalize on nonpublic information through the purchase or sale of securities." 521 U.S. at 652. It is an unsupportable extrapolation to state that this language stands for the proposition that "[a]s far back as [*O'Hagan*] . . . there has been support for the notion that the elements for insider trading under [the two theories] should be the same." *Defs.' Mem.* at 5 n.1.

[3] The Eleventh Circuit is the only federal appellate court that has held that a misappropriation case requires a showing of personal benefit. *See SEC v. Yun*, 327 F.3d 1263, 1274-80 (11th Cir. 2003) (stating that it was expressly disagreeing with the Second Circuit's approach in *Libera*).

More recent Second Circuit opinions do not squarely address this issue and do not hold otherwise. Although the Second Circuit in *SEC v. Obus* listed personal benefit as an element of tipper liability in a misappropriation case, it suggested that such a personal benefit is inherent when a tipper misappropriates inside information "because the act of misappropriation itself is deceitful." 693 F.3d 276, 286–87 (2d Cir. 2012). *Cf. United States v. Whitman*, 904 F. Supp. 2d 363, 371 n.6 (S.D.N.Y. 2012) (noting that *Obus* was "somewhat Delphic" as to whether the tipper's personal benefit is an element of a misappropriation theory case). The government's case in *Newman* was based solely on the classical theory, and as such, the opinion's passing reference to the elements under both theories being the "same" is dictum. 773 F.3d at 446.

Several district courts in the Second Circuit, including this one, have correctly observed that there is no personal benefit requirement in misappropriation cases, the later ones citing *Libera* and *Falcone*. *See Whitman*, 904 F. Supp. 2d at 370 ("[T]he tippee's knowledge that disclosure of the inside information was unauthorized is sufficient for liability in a misappropriation case."); *SEC v. Lyon*, 605 F. Supp. 2d 531, 548 (S.D.N.Y. 2009) (rejecting argument that misappropriation liability requires the receipt of personal benefit and noting that "the Second Circuit has declined to impose a 'benefit' requirement in misappropriation theory cases"); *SEC v. Willis*, 777 F. Supp. 1165, 1172 n.7 (S.D.N.Y. 1991) ("[T]he misappropriation theory does not require a showing of a benefit to the tipper."); *SEC v. Musella,* 748 F. Supp. 1028, 1038 n.4 (S.D.N.Y. 1989) (same). *But see United States v. Conradt,* 2015 WL 480419 (S.D.N.Y. Jan. 22, 2015); *Onyx*, 2014 WL 5026153, at *5.[4]

[4] The decisions in *Conradt* and *Onyx* are not binding on this Court. *Conradt*, in a four-page decision with little analysis, acknowledged that it is unclear whether *Newman* specifically resolved whether personal benefit is required in misappropriation cases. *Conradt*, 2015 WL 480419, at *1 (stating that *Newman's* application to misappropriation cases could be considered

Under this same rationale, this Court should find that the misappropriation theory does not require the tipper receive a personal benefit, and therefore that downstream tippees in misappropriation cases are not required to have knowledge of the tipper's personal benefit.

II. THE AMENDED COMPLAINT PLEADS THAT MARTIN OBTAINED A PERSONAL BENEFIT FROM TIPPING.

Even if the Commission were required to demonstrate under the misappropriation theory that Martin received a personal benefit from tipping, the Amended Complaint sufficiently alleges facts to satisfy that element. As discussed below, the Amended Complaint contains sufficient "factual content" to allow "the court to draw the reasonable inference" that Martin received a personal benefit from tipping, both under the standard established in *Dirks*, and under *Newman*.[5]

A. The Amended Complaint's Allegations that Martin and Conradt were "Friends" is Sufficient Under the Standard Established by the Supreme Court in *Dirks.*

The Amended Complaint alleges that Martin and Conradt are friends, which is sufficient to plead "personal benefit." *See* Am. Compl. ¶ 56. *Dirks* held that tipping a friend who trades is equivalent to the tipper trading on the information and giving the trading profits to the friend, which is obviously illegal. *See Dirks*, 463 U.S. at 659, 663-64 (*citing* Exchange Act § 20(b), 15

"emphatic dicta.") And *Onyx* did not squarely address this argument. *Onyx*, 2014 WL 5026153, at *5 (simply citing *Obus* and *Dirks* and listing personal benefit as an element of insider trading claims).

[5] The Commission notes that *Newman* is not final as the mandate has not been issued. The United States Department of Justice, joined by the Commission as *amicus curiae*, has petitioned the Second Circuit for rehearing or rehearing *en banc* in *Newman*. *See* FED. R. APP. P. 41(c), advisory committee's note on 1998 amendments ("A court of appeals' judgment or order is not final until issuance of the mandate; at that time the parties' obligations become fixed."). The rehearing petition stayed the mandate and acts to "suspend the finality of the court of appeals' judgment." FED. R. APP. P. 41(d)(1), advisory committee's note on 1998 amendments.

U.S.C. § 78t(b), which prohibits securities law violations committed indirectly through another person). This friendship permits the inference that Martin provided the Inside Information to Conradt in lieu of trading himself and giving Conradt the proceeds.

Newman, which addressed the sufficiency of evidence after convictions and not the sufficiency of a pleading, is not binding precedent to the extent that it is construed to hold that the government may not "prove the receipt of a personal benefit by the mere fact of a friendship." 773 F.3d at 452. Such a reading contradicts *Dirks* and the previous panel decisions in *Obus* and *Warde* holding that the fact that the tipper and tippee were "friends" is "sufficient to send to the jury the question of whether [the tipper] received a benefit from tipping." *Obus*, 693 F.3d at 291; *accord SEC v. Warde*, 151 F.3d 42, 48-49 (2d Cir. 1998) (concluding that the "close friendship between [the insider] and [the recipient of the tip] suggests that [the] tip was 'inten[ded] to benefit' [the recipient], and therefore allows a jury finding that [the] tip breached a duty under § 10(b)"). Because the decision in *Newman* came from a single panel, and not the entire *en banc* Court, it cannot overrule *Warde* and *Obus*. *See United States v. Wilkerson*, 361 F.3d 717, 732 (2d Cir. 2004). Indeed, to the extent that this portion of *Newman* conflicts with other panel decisions, "the earlier of two conflicting panel decisions" in *Warde* (decided in 1998) and *Obus* (2012) "must control" the later panel decision in *Newman* (2014). *United States v. Shellef*, 718 F.3d 94, 110 (2d Cir. 2013) (emphasis added); *see*, *e.g.*, *Sousa v. Roque*, 578 F.3d 164, 173 n.7 (2d Cir. 2009).[6]

[6] *See generally* 13 Charles Alan Wright & Arthur R. Miller, *Fed. Prac. & Proc. Juris.* § 3506, n.19 (3d ed. 2014) ("Despite the general rule requiring that a panel follow the precedent set by another panel in an earlier case, conflicts of authority do occasionally arise within a circuit. When this happens, the better rule is the earliest decision will be treated as precedential.") (collecting authorities, emphasis added).

B. The Amended Complaint's Allegations Satisfy *Newman* in Four Different Ways.

Even under *Newman* the Amended Complaint adequately pleads that Martin received a personal benefit from tipping Conradt because the allegations permit the inference that: (1) Martin and Conradt shared a "meaningfully close personal relationship;" (2) Martin intended to benefit Conradt by tipping him; (3) Martin and Conradt had a history of personal favors; and (4) Martin tipped Conradt as part of a *quid pro quo*. Am. Compl. ¶¶ 57-60, 63.

First, the Amended Complaint alleges Martin and Conradt were both friends and roommates, which satisfies *Newman* because they shared a "meaningfully close personal relationship." 773 F.3d at 452; *see also United States v. Riley*, No. 13-CR-339 (VEC), 2015 WL 891675, at *5 (S.D.N.Y. Mar. 3, 2015) (stating that a tip of inside information given to "maintain[] or further[] a friendship" is sufficient to satisfy *Newman's* personal benefit requirement). From October 2008 until approximately fall 2010, Martin and Conradt were friends and roommates in a New York City apartment, sharing common space and socializing. Am. Compl. ¶ 56. Conradt took the lead in organizing and paying shared expenses, and resolving problems. He paid the apartment bills, including cable and internet, power, and cleaning service, and then asked Martin and a third roommate to reimburse him for their portion of these expenses. *Id.* ¶ 57. He also negotiated a rent reduction with their landlord that lowered Martin's monthly rent from $1,800 to $1,500; renegotiated the cable bill for a 25% savings; hired a cleaning service; and arranged for the repair of a "buzzer," a ceiling leak, and wall outlets. *Id.* ¶ 58.

In contrast, the tippers and initial tippees in *Newman* were not roommates, and did not have such a close relationship. One *Newman* tipper and his initial tippee were "not 'close' friends"; the other pair was merely "'family friends' that had met through church." 773 F.3d at

452. Even defendants recognize that under *Newman*, "personal benefit" includes the value one obtains from making a gift of confidential information to a trading relative or close friend. *Defs.' Mem.* at 7 n.4.

Second, the Amended Complaint contains allegations that Martin intended to benefit Conradt by passing him the information. Under *Newman*, the inference of personal benefit is sufficient where there is evidence of the tipper's "intention to benefit the [tippee]." 773 F.3d at 452 (*quoting United States v. Jiau*, 734 F.3d 147, 153 (2d Cir. 2013)). The "intention to benefit the tippee" is also consistent with *Warde*, 151 F.3d at 48-49, and *Dirks*, 463 U.S. at 664. As alleged, on or about June 20, 2009, Martin was arrested and charged with assault after he was involved in a street altercation outside Grand Central Station. Am. Compl. ¶ 59. Conradt helped Martin with this situation that Martin believed could threaten his ability to legally stay in the United States. *Id.* ¶ 59. On or about June 22, 2009, just four days before Conradt first purchased SPSS securities on the basis of the Inside Information about the SPSS acquisition, Conradt called a friend who was clerking for a judge to help advise Martin on how to deal with his arrest. *Id.* ¶ 60. Subsequently, Dallas, Martin, Conradt, and Conradt's friend discussed the best legal strategy and potential attorneys to hire for Martin. *Id.*

In late July, after the public announcement of the SPSS acquisition, during a conversation about their respective trading and profits from the Inside Information, Martin again thanked Conradt for his prior assistance with the criminal legal matter and Martin told Conradt he was happy that Conradt profited from the SPSS trading because Conradt had helped him. *Id.* ¶ 63. That Martin allegedly told Conradt he was happy Conradt had traded for a profit on the Inside Information demonstrates Martin's intention to benefit Conradt, and that Martin intended or

reasonably expected that Conradt would trade on the information, which is sufficient to plead personal benefit under *Newman*.

Third, the allegations in the Amended Complaint demonstrate a "history of loans or personal favors between" Martin and Conradt, which sufficiently supports the inference that Martin gave Conradt inside information as a personal favor for personal benefit. *Newman*, 773 F.3d at 453. As described above, Martin and Conradt had a history of personal favors. Am. Compl. ¶¶ 57-60. This supports an inference that Martin also gave Conradt the Inside Information as a personal favor.

Fourth, the allegations in the Amended Complaint even satisfy defendants' unreasonable reading that *Newman* requires an actual *quid pro quo*. Contrary to defendants' assertion, *Newman* does not require the Commission to allege that Martin, the tipper, received a *quid pro quo* benefit for tipping Conradt. *Defs.' Mem.* at 8 ("the Complaint fails to plead any tangible benefit or *quid pro quo* that Martin received from Conradt."). In fact, nowhere does *Newman* define personal benefit so narrowly. 773 F.3d at 452 (describing the proof standard as "permissive" but discussing certain limitations). In any event, the allegations support the inference that Martin tipped Conradt as part of a "*quid pro quo*." *Newman*, 773 F.3d at 452. Further, it is "an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature," *Newman*, 773 F.3d at 452. Conradt provided Martin with legal help, a discount on rent and his cable bills, and other services that are pecuniary or of a similarly valuable nature. In exchange, Martin tipped Conradt valuable, inside information. Am. Compl. ¶¶ 56-60. Indeed, there is ample evidence from which to infer a *quid pro quo* given Martin thanked Conradt for his prior assistance with the criminal legal matter and, in the same discussion, told Conradt he was happy that Conradt profited from the SPSS trading

because Conradt had helped him. *Id*. ¶ 63. *See also Riley*, 2015 WL 891675, at *5 ("If a tip maintains or furthers a friendship, and is not simply incidental to the friendship, that is circumstantial evidence that the friendship is a *quid pro quo* relationship.")

III. THE AMENDED COMPLAINT SUFFICIENTLY PLEADS THAT DEFENDANTS KNEW OR SHOULD HAVE KNOWN THAT MARTIN BREACHED HIS DUTY AND OBTAINED A PERSONAL BENEFIT.

Defendants also argue that the Commission has failed to allege that "Payton and Durant were aware of any duty Martin breached in disclosing the information to Conradt." *Defs.' Mem.* at 11. Defendants contend the Complaint "lacks any allegation that Conradt told Defendants where the information came from or that the individual who tipped him had done so in violation of a duty." *Id.* They further argue that the Commission fails to allege that defendants "knew . . . the information was . . . divulged for personal benefit." *Defs.' Mem*. at 9. In making these arguments defendants misstate the requirement for pleading this element of tippee liability. Indeed, the well-pleaded facts of the Amended Complaint show that defendants knew or should have known that Martin breached a duty for a personal benefit when he tipped Conradt.

While the government was required in *Newman* to show that a tippee "knew" that the tipper had breached a duty and obtained a personal benefit, it is sufficient if the Commission in this civil case shows that the tippee "knew or should have known" this. Criminal liability in *Newman* required the government to "show that the defendant acted 'willfully.'" *Newman*, 773 F.3d at 447 (*quoting* 15 U.S.C. § 78ff(a)). But in a civil enforcement action the Commission is not required to show that the defendant acted "willfully" under 15 U.S.C. § 78ff(a), because that statute applies only in criminal cases. Indeed, in *Dirks*—a civil enforcement action—the Supreme Court explained that a tippee has a duty to abstain or disclose "only when the insider has breached his fiduciary duty . . . and the tippee knows or should know that there has been a

breach." 463 U.S. at 660 (emphasis added). *See also Obus*, 693 F.3d at 287-88 (confirming that the Commission need only show that the tippee "should know," similar to a "negligence standard," that the tipper breached a duty). The requirement of reckless or intentional conduct "pertains to the tippee's eventual use of the tip through trading or further dissemination of the information." *Obus*, 693 F.3d at 288.

Whether the tippee knew or should have known of the tipper's breach and personal benefit is a "fact-specific inquiry turning on the tippee's own knowledge and sophistication, and on whether the tipper's conduct raised red flags that confidential information was being transmitted improperly." *Obus*, 693 F.3d at 288; *SEC v. Musella*, 578 F. Supp. 425, 442 (S.D.N.Y. 1984) (the tippee "either knew or should have known that he was trading on improperly obtained nonpublic information"). The Commission must set forth facts under which it is plausible that defendants knew or should have known that the confidential information was obtained and transmitted improperly (and through deception). *See Obus*, 693 F.3d at 287-88 (tippee must "have some level of knowledge that by trading on the information the tippee is a participant in the tipper's breach of fiduciary duty"); *SEC v. Conradt*, 947 F. Supp. 2d 406, 412 (S.D.N.Y. 2013). The Commission need not plead that defendants knew or should have known "for certain how the information was disclosed," *Newman*, 773 F.3d at 449, or "how the initial breach of fiduciary duty occurred," *Conradt*, 947 F. Supp. 2d at 412. And "[a]n allegation that the tippee knew of the tipper's breach necessarily charges that the tippee knew that the tipper was acting for personal gain." *Newman*, 773 F.3d at 449 n.4 (*quoting United States v. Santoro*, 647 F. Supp. 153, 170-71 (E.D.N.Y. 1986), *rev'd on other grounds*, *United States v. Davidoff*, 845 F.2d 1151 (2d Cir. 1988)).

Courts have found, among others, the combination of some or all of the following allegations support the tippee "knew or should know" standard: (1) access to information; (2) timing of contact between the tipper and the tippee; (3) sophistication of the tippee; (4) timing and pattern of the trades; (5) attempts to conceal either the trades or the relationship between the tipper and the tippee; and (6) relationship between the tipper and the tippee. *See*, *e.g.*, *Warde*, 151 F.3d at 47-48 (relationship, timing and pattern of trading); *Obus*, 693 F.3d at 288, 292-93 (access, timing of contacts, sophistication, relationship); *United States v. Larrabee*, 240 F.3d 18, 21-22 (1st Cir. 2001) (all, in finding sufficient evidence for a jury verdict of guilty); *Conradt*, 947 F. Supp. 2d at 412-13 (timing of contacts, sophistication, trading, concealment). For example, in *Conradt*, premised on similar facts and parties as the Amended Complaint, the Court found that the sophistication of the tippees, and in particular, their knowledge of the securities markets and the prohibition against insider trading, combined with contemporaneous communications and after-the-fact conduct reflecting consciousness of guilt, "more than plausibly indicate that [the tippee] knew that [the tippers] had obtained and transmitted the information to him improperly." 947 F. Supp. 2d at 413. As discussed below, the allegations in the Amended Complaint similarly support the requisite inferences, which is all that they must do at the pleading stage. *See Walker*, 717 F.3d at 124 (on motion to dismiss, court should not "assay the weight of the evidence which might be offered in support thereof"); *DiFolco*, 622 F.3d at 113 (same); *Elastic Wonder*, 2015 WL 273691, at *1 (function of motion to dismiss is not to weigh evidence).

Access to information. Martin learned the Inside Information from Dallas. *See* Am. Compl. ¶¶ 48-53. Martin misappropriated the information from his friend and tipped that

information to Conradt. *Id.* ¶ 61. Conradt tipped the Inside Information to defendants Payton and Durant. *Id.* ¶¶ 70-74.

Timing of the defendants' communications. Soon after Conradt first told defendants that SPSS was likely going to be acquired and that the information was confidential, the defendants referred vaguely to the information in written communications and the men did not refer to it as "SPSS." *Id.* ¶¶ 70-73 (Conradt and Payton exchange an instant message where Conradt asked whether Payton had begun to buy options or the stock "for our horse."). Over the next month or so Durant repeatedly asked Conradt for additional information on the SPSS Acquisition and ultimately, prior to July 20, 2009, Conradt provided to both defendants more specific information, including reassurance as to the continuing viability of the tip, the names of the parties to the transaction, and that the transaction would happen soon. *Id.* ¶¶ 74, 75. The defendants immediately traded in SPSS securities, betting that the price of the stock would increase. *Id.* ¶¶ 75-78

Defendants' sophistication. Payton and Durant were licensed securities professionals employed in the securities industry, and sophisticated investors who had knowledge of the securities markets, how the market reacted to material information, and the consequent value of material, nonpublic information, and the prohibition against insider trading. Am. Compl. ¶¶ 12, 13, 90. Indeed, as part of their employment in the securities industry, both defendants signed certifications affirming their knowledge and understanding of policies and procedures regarding insider trading. *Id.* ¶ 90.

The timing, pattern, and type of defendants' trades. After Conradt provided defendants with additional, specific information about the transaction, *Id.* ¶ 74, defendants immediately

purchased large amounts of options with strike prices greater than the current price of SPSS stock, thereby anticipating that the price of SPSS stock would go up. *Id.* ¶¶ 75-78.

Defendants' attempts to conceal their trading. The day the SPSS Acquisition was announced, defendant Durant, Conradt, and one other individual went to lunch, and Durant paid cash to expressly avoid leaving a paper trail. Am. Compl. ¶ 81. Later that night, defendants met with the other men who had traded based on the tip and agreed that they would not discuss their trading with anyone. *Id.* ¶ 82. Soon after, Payton transferred his SPSS securities from an account at his employer to a new brokerage firm and did not disclose to that firm his employment in the securities industry, thereby circumventing any controls the new firm had to monitor the activities of securities industry employees or to notify his employer of the same. *Id.* ¶ 83. Moreover, defendants' concealment of their illegal trading from their employer upon questioning about their trading further supports the inference that they knew or had reason to know that the SPSS information had been passed in breach of a duty and for a personal benefit. *Id.* ¶¶ 83-85. *See Warde*, 151 F.3d at 49 (deceptive behavior, such as concealing trades, supports the inference of illegal trading). *Cf. Obus*, 693 F.3d at 293 (finding defendant's conduct after the tip, including his offer to employ the tipper if the tipper was fired, relevant to whether he knew or should have known that the information was obtained in breach of a duty); *Larrabee*, 240 F.3d at 23 (defendants' efforts to conceal their contacts and the nature of their relationship support an inference of trading on illegal insider information).

Relationship between the tipper and the tippee. Defendants actually knew that Martin and Conradt were friends and roommates, Am. Compl. ¶ 68, and Conradt told the defendants that the Inside Information came from Martin, *id.* ¶ 70. Indeed, Durant repeatedly asked Conradt whether Martin had given him any additional information. *Id.* ¶ 74. *See also Def. Mem.* at 7 n.4

(the concept of personal benefit includes the benefit one would obtain from simply making a gift of confidential information to a trading relative or friend). This is in sharp contrast to *Newman*, where the tippees "knew next to nothing" about the tipper, were unaware of the "circumstances" of how the information was obtained," and "did not know what the relationship between the [tipper] and the first-level tippee was." 773 F.3d at 453-54.

In sum, the allegations in the Amended Complaint more than plausibly indicate that defendants knew or should have known that the Inside Information had been obtained and transmitted to them improperly.

IV. THE AMENDED COMPLAINT CLEARLY AND SUFFICIENTLY ALLEGES DURANT'S PARTICIPATION IN THE ILLEGAL CONDUCT.

Finally, Durant argues that the Commission failed to allege facts with sufficient particularity to show Durant's involvement in the illegal conduct, claiming Durant to be in the "impossible position of not knowing who the [Commission] is going to try to prove provided Durant with the information and whether the [Commission] is alleging fraud at all." *Defs.' Mem.* at 11-12. To the extent Durant was confused by the pleadings in the Complaint, there is no basis for any such argument regarding the Amended Complaint. The allegations in the Amended Complaint are more than sufficient to satisfy Rule 9(b). The Amended Complaint alleges that:

> On or before July 1, 2009, Conradt learned that RR1 had told defendant Durant the Inside Information that Conradt had previously told RR1. Conradt then personally told defendants Payton and Durant that his roommate Martin had told him that SPSS was likely going to be acquired. Knowing that Conradt was Martin's roommate, Payton and Durant did not ask Conradt why Martin told Conradt the Inside Information and did not ask Conradt how Martin learned this information.

Am. Compl. ¶ 70. Over the next few weeks, Durant repeatedly sought additional information from Conradt. *Id.* ¶ 74. Then prior to July 20, 2009, Conradt provided to Durant (and Payton) additional, more specific information, confirming the continued viability of the SPSS

Acquisition, identifying the parties to the SPSS Acquisition and indicating that the transaction would occur "soon." *Id.* ¶ 74. Following this later tip, Durant placed bets in the form of call options, clearly expecting the price of SPSS stock to rise over the next few weeks, which, in fact, it did upon the announcement. *Id.* ¶¶ 75, 76.

Given the specific allegations in the Amended Complaint, there can be no serious dispute that the Amended Complaint states a claim for insider trading against Durant. *See Onyx*, 2014 WL 5026153, at *4 (stating that Rule 9(b) "may be relaxed to allow a plaintiff to plead facts that imply the content and circumstances of an insider tip.") (citations omitted).

CONCLUSION

For the reasons set forth above, the defendants' motions to dismiss should be denied.

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Respectfully Submitted,

SECURITIES AND EXCHANGE COMMISSION

s/ Catherine E. Pappas
David L. Axelrod
Catherine E. Pappas
A. Kristina Littman
Counsel for Plaintiff
One Penn Center
1617 JFK Blvd, Suite 520
Philadelphia, PA 19103
(215) 597-3100