13-1837-cr(L)

13-1917-cr(con)

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

UNITED STATES OF AMERICA,

Appellee,

—against—

JON HORVATH, DANNY KUO, HYUNG G. LIM, MICHAEL STEINBERG,

Defendants,

TODD NEWMAN, ANTHONY CHIASSON,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF DEFENDANT-APPELLANT ANTHONY CHIASSON IN OPPOSITION TO THE UNITED STATES OF AMERICA'S PETITION FOR REHEARING AND REHEARING *EN BANC*

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INTRODUCTION

In the classic folk tale "Chicken Little," an acorn falls on the protagonist, and Chicken Little goes to warn the King that "the sky is falling." The government's rehearing petition echoes Chicken Little's complaint, though its tone is less that of a frightened hen and more that of a petulant rooster whose dominion has been disturbed. The petition asserts variously that the "missteps" in the Court's Opinion in this case were "unprecedented," "unfounded," "untenable," "confounding," "incorrect," "erroneous," "mistaken," and "wrong." As a consequence, the government writes, the Opinion "redefin[ed]" the law of insider trading and could permit culpable conduct to go unpunished "contrary to all previous understanding of the securities laws . . . ." Pet. 23, 23 n.5.[1] The petition concludes with the warning that investor confidence will suffer because individuals will perceive that the exploitation of nonpublic information for personal gain is permissible. *Id.* at 24.

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[1] References to the government's petition for rehearing are cited as "Pet. __." References to Todd Newman's brief in opposition to the government's petition for rehearing are cited as "Newman Opp'n Br. __." References to the Securities and Exchange Commission's amicus brief in support of the government's petition for rehearing are cited as "SEC Amicus Br. __." References to the Court's decision are cited as "Opinion __." References to the trial transcript are cited as "Tr. __." References to the Joint Appendix on appeal are cited as "A-__."

Respectfully, this is nonsense. The Opinion does not purport to redefine the law of insider trading and it does no such thing. It faithfully follows and applies the definition of "personal benefit" that the Supreme Court first discussed in *Dirks* v. *SEC*. 463 U.S. 646, 662-63 (1983). Relying on *Dirks*, the Opinion holds—consistent with almost all of the prior district court decisions on point[2]—that a tippee must *know* that an insider has disclosed material nonpublic information in exchange for personal benefit in order to commit insider trading. The government now explicitly declines to challenge this holding. Pet. 2.

Given the government's decision not to challenge the Opinion's key legal ruling, there is no basis upon which to rehear this case. As we argue below, the Opinion's discussion of "personal benefit" for purposes of tipper liability follows and relies upon existing precedent, and works no change in the law, let alone the drastic change to which the government alludes in its "Chicken Little" argument. The application of the law to the evidence, and the conclusion that the government did not prove at trial that the Dell and NVIDIA insiders exchanged information for personal benefit, is a garden-variety analysis of a unique factual record that has no broad importance. In any case, the Court's analysis was correct. Further, the

[2] The only contrary district court decisions, as the Opinion notes, were rendered by Judge Sullivan in this and a related case. Opinion 17 (citing *United States* v. *Steinberg*, No. 12-121, 2014 WL 2011685 at *5 (S.D.N.Y. May 15, 2014) (Sullivan, J.); *United States* v. *Newman*, No. 12-121 (S.D.N.Y. Dec. 6, 2012) (Sullivan, J.)).

government's quarrel with the Opinion's description of "personal benefit" is irrelevant to the final result. Under *any* formulation of "personal benefit," there was no evidence that Anthony Chiasson knew that the insiders were receiving a benefit or even promoting a friendship. The Court's analysis of the lack of evidence on this issue was correct. The government's rehearing petition does not point to any new or mistaken facts regarding Chiasson's knowledge, but simply repeats the same unpersuasive factual arguments that it made to the Panel. This kind of small-caliber factual parsing does not warrant rehearing. Finally, we respond briefly to the government's "sky is falling" argument. It is not true that the Opinion threatens well-founded law enforcement efforts, civil or criminal, aimed at insider trading. To the extent that there is confusion regarding the law of insider trading, the blame rests not with courts, which simply decide the cases brought before them, but on the government and the SEC, which have advocated discredited legal theories and failed to promulgate regulations that would resolve ambiguities in a landscape that has been charted by courts and market participants for many years without a statutory or regulatory definition of "insider trading."

ARGUMENT

I. THE OPINION'S DISCUSSION OF "PERSONAL BENEFIT" FOLLOWED EXISTING LAW

The government (and the SEC as *amicus*) complains most loudly about the Opinion's discussion of "personal benefit," arguing that the Panel has

"redefine[d]" this requirement in a significant way. Pet. 2. The argument focuses on a single sentence in the Opinion: "To the extent *Dirks* suggests that a personal benefit may be inferred from a personal relationship between the tipper and tippee, where the tippee's trades 'resemble trading by the insider himself followed by a gift of the profits to the recipient,' we hold that such an inference is impermissible in the absence of 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." Opinion 22 (quoting *Dirks*, 643 U.S. at 664). According to the government, this language contravenes the holding in *Dirks* that "a gift of confidential information to a trading relative or friend" can satisfy the personal benefit requirement. *See* Pet. 13; *see also* Pet. 12-14 (claiming language is inconsistent with various Court of Appeals decisions discussing gift theory of benefit).

On the contrary, the Court's Opinion is entirely consistent with *Dirks*. The core holding of *Dirks* is that an insider's disclosure of confidential information constitutes a fiduciary breach triggering insider trading liability only if the insider provides the information "to an outsider for the . . . improper purpose of exploiting the information for [the insider's] personal gain." 463 U.S. at 659. That is, the purpose of the insider's disclosure must be to secure some "'personal advantage'" so that "the insider personally will benefit, directly or indirectly, from his

disclosure." 463 U.S. at 662 (quoting *In re Cady, Roberts & Co.*, 40 S.E.C. 907, 912 n.15 (1961)). Of course, where there is an explicit *quid pro quo* exchange, the tipper commits a fraudulent breach. Even absent an explicit *quid pro quo*, a "meaningfully close relationship" between the tipper and the tippee may warrant an inference that the tipper anticipates a potential gain that is "objective and consequential." If so, it is appropriate to view the tipper as having committed fraud because the tipper has breached his fiduciary duties in anticipation of personal benefit. Under *Dirks* the tipper's disclosure of confidential information is tantamount to self-dealing, and exposes the tipper to liability for securities fraud. But where the tippee is nothing more than a casual associate, or where the disclosure of information is not connected to an existing personal relationship, the inference of potential gain to the tipper may not be warranted in the absence of other facts suggesting at least an implicit *quid pro quo*.

The government complains that the Panel's reference to a "meaningfully close personal relationship" and to an exchange of information for potential gain "effectively upended *Dirks*." *See* Pet. 12, 14. But in the very same paragraph the Panel made crystal clear that it was following and reaffirming *Dirks*, and that a gift of confidential information to a friend with the intent that the friend trade and profit on the information also can lead to liability. The Opinion twice observes that the government can satisfy the benefit element by demonstrating that a tipper

disclosed the information to a friend so that the friend can trade on it. First, the Court pointed out that personal benefit includes "'*the benefit one would obtain from simply making a gift of confidential information to a trading relative or friend*.'" Opinion 21 (quoting *United States* v. *Jiau*, 734 F.3d 147, 153 (2d Cir. 2013), which quotes *SEC* v. *Obus*, 693 F.3d 276, 285 (2d Cir. 2012), and *Dirks*, 463 U.S. at 663) (emphasis added). Later, the Court explained that a relationship generates the requisite exchange if it suggests a "*quid pro quo*" or "'suggests . . . *an intention to benefit the [tippee]*.'" Opinion 22 (quoting *Jiau*, 734 F.3d at 153, which quotes *Dirks*, 463 U.S. at 664) (emphasis added). In short, contrary to the government's argument, the Opinion leaves intact the rule that the government can prevail if it shows that the tipper made a gift of material nonpublic information to a friend, anticipating and intending that the friend would trade on the information and earn trading profits. There is liability in such cases either because the facts warrant an inference that the tipper expects a tangible *quid pro quo* or because the result is substantially the same as the tipper having made a direct profit by trading on information and then giving the money to the tippee. As the *Dirks* court noted, the insider's conduct in such cases involves both breach of fiduciary duty and the exploitation of confidential corporate information to benefit the recipient. *Dirks*, 463 U.S. at 662. However, the mere existence of a friendship, and the disclosure of information to a friend, is not enough. There must be either the expectation of a

quid pro quo or the intention that the recipient trade on the information and reap profits. This analysis is faithful to *Dirks* and its progeny.[3]

Under the government's apparent view of the law, disclosure of confidential information to anyone who might be viewed as the insider's "friend" amounts to fraud. But that is not what *Dirks* held, and the Panel correctly observed that, "[i]f this was a 'benefit,' practically anything would qualify." Opinion 21. In its Petition, as in its prior briefing, the government ignores the central point of *Dirks*, which identifies the tipper's exploitation of confidential information for personal

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[3] In the cases the government cites, the benefit at issue either involved pecuniary benefit or an actionable gift of information to be used for trading profits. Moreover, in some of the cases personal benefit was not litigated but the "gift to a trading relative or friend" was merely mentioned in passing. For example, in *Jiau*, this Circuit's most recent pre-*Newman* case applying the personal benefit requirement, the benefits to one tipper included "meals at restaurants" and "gifts including an iPhone, live lobsters, a gift card, and a jar of honey," and the benefit to the other tipper included access to an investment club that provided "the opportunity to access information that could yield future pecuniary gain." 734 F.3d at 153; *see* Opinion at 22 (distinguishing *Jiau*). *See also SEC* v. *Warde*, 151 F.3d 42, 48 (2d Cir. 1998) (tipper and tippee had a "close friendship"; they lived across the country from each other but nonetheless socialized "several times a year" whenever one traveled to the other's state, *see S.E.C.* v. *Downe*, 969 F. Supp. 149, 152 (S.D.N.Y. 1997)); *SEC* v. *Maio*, 51 F.3d 623, 627 (7th Cir. 1995) (tipper and first-level tippee had a "close friendship[]," tipper had loaned tippee $250,000, and tippee had recommended that tipper be appointed president of mutual friend's company); *SEC* v. *Rocklage*, 470 F.3d 1, 4 (1st Cir. 2006) (tippee was tipper's brother; dicta with generic reference to gift theory). For example, as the Court pointed out, in *SEC* v. *Yun*, 327 F.3d 1263 (11th Cir. 2003) (cited by SEC Amicus Br. at 10), the "tipper and tippee worked closely together in real estate deals and commonly split commissions on various real estate transactions." Opinion 22.

benefit as the gravamen of culpable insider trading. Rather than accepting this rule of law, which has been stated more than once by the Supreme Court, the government apparently wishes to water down the meaning of "personal benefit" so that, as a practical matter, it can bring insider trading charges whenever someone trades on material nonpublic information that is disclosed without authorization by a company insider. It would be sufficient for the prosecutors, apparently, if an insider provided information to a "church friend" or perhaps even a Facebook "friend," without intending that the friend profit by trading on the information. This conduct may violate corporate policy or the SEC's Regulation FD, but it is not fraudulent self-dealing under *Dirks* and its progeny, and does not open the door to prosecution for insider trading. The Panel's Opinion properly recognizes this principle, and reinforces the line that the Supreme Court has drawn to separate legal from illegal trading.[4] The government does not like where that line has been drawn, but it ought not criticize this Court for adhering to settled principles of insider trading jurisprudence.

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[4] As the Court explained: "Although the government might like the law to be different, nothing in the law requires a symmetry of information in the nation's securities markets. The Supreme Court explicitly repudiated this premise not only in *Dirks*, but in a predecessor case, *Chiarella* v. *United States*." Opinion 16. Thus, "insider trading liability is based on breaches of fiduciary duty, not on informational asymmetries," *id.*, and under *Dirks*, "the corporate insider has committed no breach of fiduciary duty unless he receives a personal benefit in exchange for the disclosure." *Id.* at 13-14.

II. THERE IS NO REASON TO RECONSIDER THE COURT'S RULING THAT THE EVIDENCE OF PERSONAL BENEFIT WAS INSUFFICIENT IN THIS CASE

After describing the law regarding the "personal benefit" requirement, and opining correctly that the requirement was "permissive" but not entirely without substance, the Court reviewed the trial evidence. Opinion 21. It concluded that the evidence, even considered under an "exceedingly deferential" standard of review, "was simply too thin to warrant the inference that the corporate insiders received any personal benefit in exchange for their tips." *Id.*

There is no reason for the full Court to revisit this fact-based conclusion, which rests on a careful review of a particular trial record. *See* Newman Opp'n Br. 3-4. If the Court were to entertain en banc review whenever a party disagreed with a Panel decision on an issue of evidentiary sufficiency, the Second Circuit's work would grind to a halt. *See Watson* v. *Geren*, 587 F.3d 156, 160 (2d Cir. 2009) (per curiam opinion concurring in denial of petition for rehearing en banc) ("[I]f the legal standard is correct, then the full court should not occupy itself with whether the law has been correctly applied to the facts. If that were the appropriate course, then our dockets would be overloaded with en banc polls contesting a panel's examination of particular sets of facts." (citation omitted)).

In any case, the Panel decision was correct, and should not be reconsidered. Neither of the insiders whose conduct was at issue was prosecuted for insider

trading, and neither appeared as a trial witness. The prosecution was therefore hoping to clobber the remote tippees with a hollow bat. Though the government claimed that the Dell insider disclosed information to a friend in exchange for "career advice," the record was inadequate to support the claim. The initial tippee, Sandy Goyal, testified that he and Rob Ray (the Dell insider) were "not very close or personal." (Tr. at 1411). They were merely two alumni of the same business school who casually kept in touch and talked about their careers. (Tr. at 1390-91, 1411). While they worked together at Dell for two years after graduation, they did not socialize even once between 2004 and 2010, a span of years that covered the entire time during which Ray was speaking to Goyal about Dell's financial performance. (Tr. at 1512-13).

The government never proved that Ray provided Goyal with material nonpublic information about Dell in order to get career advice. The prosecutors' decision not to call Ray as a witness spoke volumes: Ray had proffered that he never connected Goyal's career advice to the Dell information in his own mind, and Goyal's advice "did not influence the manner in which [Ray] performed his duties at Dell." (A-147). Goyal testified that he gave Ray career advice for "one, one and a half years" before Ray started providing any information about Dell. (Tr. at 1514). And Goyal confirmed that Ray did not once link the Dell information to Goyal's career advice in their conversations. (Tr. at 1514). The

government dismisses this as "unsurprising[]," Pet. 18, but it illustrates the lack of proof that Ray gave Goyal confidential Dell information *in exchange for* career advice.[5]

As for the NVIDIA tips, it was undisputed at trial that Choi, the NVIDIA insider, did not receive anything from Lim (the initial tippee) in exchange for NVIDIA information. (Tr. at 3067-68).[6] The government's theory was that Choi and Lim were close friends, and that Choi's information was a gift to a trading friend. As the Panel rightly held, however, Choi and Lim were merely casual acquaintances. Lim described Choi as a "family friend" whom he knew from church services, "other occasional church activities," and family picnics. He occasionally had lunch with Choi. (Tr. at 3032-33). Lim was the one who elicited the NVIDIA information from Choi, and he did so through vague questions "about how the quarter is doing." (Tr. at 3034). Lim testified that he never told Choi that

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[5] The government argues that the career advice Goyal gave Ray was more detailed and extensive than the advice he gave to others. Pet. 16-17. But this is irrelevant; the issue is not *Goyal's* motive in talking to Ray, but *Ray's* motive for giving Dell information to Goyal. And Goyal testified that he would have given the same advice and input to "other people too if they asked [him]," but "[Ray]'s the only one that called me" (Tr. at 1630), and that he would have given Ray career advice even if Ray was not giving him information about Dell. (Tr. at 1515).

[6] The government's discussion of money exchanged between downstream tippees, Pet. 18-19, is completely irrelevant to whether the NVIDIA tipper received a benefit.

he wanted the information so he could trade on it, and, in fact, Lim did not trade on the NVIDIA information that underlay the substantive count based on NVIDIA trading. (Tr. at 3069, 3077-78). Nor did Lim ever tell Choi that he would pass the information on to others for them to trade on it. (Tr. at 3069). There was, in short, no evidence to show that Choi intended to make a gift of trading profits to a close friend.

III. THERE IS NO REASON TO REVISIT THE COURT'S CONCLUSION THAT THE GOVERNMENT OFFERED "ABSOLUTELY NO EVIDENCE" THAT CHIASSON KNEW THAT INSIDERS WERE EXCHANGING INFORMATION FOR THEIR PERSONAL BENEFIT

Even if the Opinion had materially changed the law regarding "personal benefit"—which it did not—and even if the government had offered sufficient proof that the insiders were exchanging confidential information for personal benefit—which it did not—there still would be no basis to reconsider the Court's conclusion that the charges against Chiasson had to be dismissed. After fighting tooth and nail for several years, the government finally has decided not to challenge the ruling that it can convict a tippee only if it proves that the tippee *knew* that an insider disclosed confidential information for personal benefit. Pet. 2.

There was no such proof in this case. The Panel received extensive briefing and argument on the facts and concluded that the prosecutors had not come close to meeting their burden. The Opinion recites that "the Government presented

absolutely no testimony or any other evidence" showing that Chiasson knew that the "insiders received any benefit in exchange for [their] disclosures, or even that . . . Chiasson consciously avoided learning of these facts." Opinion 24. There is no reason to reconsider this conclusion, and at least three compelling reasons why reconsideration is unwarranted.

First, there is the intensely fact-specific nature of the Opinion's conclusion that the evidence of Chiasson's knowledge was insufficient. This inquiry turns not on any significant question of law or policy, but on the granular parsing of the exhibits and testimony introduced at the trial. Questions of this nature are particularly unsuited for en banc consideration, and the appellate rules do not contemplate en banc rehearing regarding such issues. En banc treatment, disfavored in general, is intended for issues of "exceptional importance." Fed. R. App. P. 35(a)(2); *see generally* Jon O. Newman, *In Banc Practice in the Second Circuit: The Virtues of Restraint*, 50 Brook. L. Rev. 365, 382 (1984) ("The Second Circuit's self-discipline in holding to a minimum the number of appeals reheard in banc is, in my view, a distinct benefit to the court, the bar, and the development of the law.") However important the issue of evidentiary sufficiency may be for Chiasson personally, it is not important to anyone else.

Second, the Panel's conclusion that there was insufficient evidence of Chiasson's knowledge was manifestly correct. This was not even a close issue.

The Panel concluded unanimously that there was "absolutely no testimony or any other evidence" that Chiasson knew of personal benefit flowing to the Dell or NVIDIA insiders. Opinion 24. It was undisputed at trial that all of Chiasson's knowledge about the inside information came to him from his analyst, Adondakis, who testified as a government witness. As the Opinion correctly notes, "Adondakis said that he did not know what the relationship between the insider and the first-level tippee was, nor was he aware of any personal benefits exchanged for the information, nor did he communicate any such information to Chiasson." *Id.* Whatever may be the dubious significance of the "career advice" given to the Dell insider, or the "friendship" between the NVIDIA insider and his initial tippee, Chiasson knew absolutely nothing about those matters. Chiasson's complete lack of knowledge was affirmatively established by Adondakis' testimony, and the government did not offer a scintilla of contrary proof.

Third, the Petition presents no new evidence that the Panel overlooked or misstated in concluding that there was a failure of proof with respect to Chiasson's lack of knowledge. As to NVIDIA, the government appears to have thrown in the towel. In the section of the Petition addressing the sufficiency of the evidence regarding knowledge of personal benefit, the government does not even mention

NVIDIA.[7] As to Dell, the government's recitation of facts contains nothing new and nothing remotely suggesting that Chiasson knew that a Dell insider was exchanging information for "career advice" or any other personal benefit. The prosecutors refer to Adondakis' testimony that he told Chiasson that the information was coming from "someone within Dell." Pet. 20 (citing Tr. 1708). This fact added nothing to the mix of what Chiasson knew. Any information about Dell's financial performance of course emanated in the first instance from Dell, but Chiasson did not know the Dell insider, or anything about the insider's position or motives for speaking about the company's prospects. Particularly in an environment where, as the Opinion correctly observed, "the corporate insiders at Dell and NVIDIA regularly engaged with analysts and routinely selectively

[7] In its Statement of the Case, the government writes that "Chiasson . . . knew that the NVIDIA figures were coming from an NVIDIA 'contact' . . . who 'went to church with' a friend of Kuo's." Pet. 7. This sentence conflates two facts, only one of which was known to Chiasson. It is true that Adondakis told Chiasson about a "contact" for NVIDIA information, and it is also true that the NVIDIA insider "went to church with" Lim, who was a friend of Kuo. But Chiasson did not know the latter fact. The trial evidence was unequivocal that Chiasson was never told about any relationship between an NVIDIA insider and anyone else. He knew only that Adondakis referred to an NVIDIA "contact." To the extent that the government intended to suggest that Chiasson knew of any friendship between the NVIDIA insider and his tippee, that suggestion is absolutely false. We trust that the conflation of Chiasson's knowledge in this sentence was the product of grammatical sloth, and not an intentional distortion of the record with respect to a significant fact.

disclosed the same type of information," Opinion 27,[8] Adondakis' reference to a source "within Dell" gave Chiasson no basis to know that the source was acting for personal gain. The same is true for the other facts to which the Petition refers. Each of those facts was discussed in the government's briefing to the Panel; it therefore suffices here simply to repeat the following discussion from Chiasson's reply brief (with cross-references to the same arguments as made in the Petition):

[8] Referring to these selective disclosures, the Petition argues that "selective disclosure of earnings would be unlawful under SEC Regulation FD, and a jury could infer that Newman and Chiasson, as sophisticated securities professionals, knew that." Pet. 21 (citation omitted). But, even assuming that Chiasson understood or should have understood that someone at Dell was violating Regulation FD, this does not mean that there was an insider acting for personal benefit and thereby committing fraud, let alone that Chiasson knew that. As we argued in our main brief, the very purpose of Regulation FD was to curb selective disclosures that are *not* made for personal benefit, and that therefore do not give rise to insider trading liability. Chiasson Br. 27-29; 47-48. An outsider who trades on information that has been selectively disclosed in violation of Regulation FD does not even violate the Regulation, which applies only to issuers and their personnel. Such trading does not *ipso facto* violate Rule 10b-5, as the government seems to suggest. By making this argument, the government betrays its confusion. It apparently believes that all corporate information must be released through legitimate, authorized channels (in which case, of course, the information is public), or the information is unauthorized and provides a basis for insider trading charges if it is used to buy or sell stock. This is simply not the law. The whole point of *Dirks* and its progeny was to reject the view that trading on material nonpublic information is illegal *vel non*, and to insist on proof of an insider's fraudulent breach of fiduciary duty for personal gain. An insider who violates Regulation FD does not automatically act for personal gain, just as a prosecutor who leaks grand jury information may violate office policy or even federal law without necessarily acting for personal benefit.

> [T]he government cites a conversation between Chiasson and a hedge fund competitor in which Chiasson declined to divulge the source of his insights about Dell's gross margins. (Gov't Br. 63)[Pet. 20.] The conversation was completely irrelevant to Chiasson's knowledge of personal benefit, but in any event there is nothing nefarious about protecting information sources from a competitor. The government also contends that Chiasson directed Adondakis to create "sham reports reflecting false reasons for the trades." (Gov't Br. 64)[Pet. 20]. But this is just government rhetoric; Adondakis did not testify that the reports were "sham" or contained "false reasons." Chiasson did not instruct Adondakis to falsify anything; the evidence was that Chiasson instructed Adondakis to put "something quick" in the firm's internal "Idea" tracing system to document the *actual* rationale for the trade (i.e., the "potl gm [potential gross margins] miss"). (A-2115). Again, this evidence was irrelevant to knowledge of insider benefit.

Chiasson Reply Br. 27.

All of the factual arguments in the Petition were presented to the Panel that heard the appeal. That all three judges found those facts unpersuasive hardly entitles the government to put the same cheap wine in a bottle with a new label and present it to the entire Second Circuit bench as fine champagne.

The prosecution is not entitled to an appellate "do over." And, in light of its complete failure to produce any evidence that Chiasson knew that company

insiders were providing confidential information for personal benefit, it is not entitled to a "do over" of the trial.[9]

IV. THE PANEL'S DECISION DOES NOT "THREATEN THE INTEGRITY OF THE SECURITIES MARKETS"

The government contends finally that the Opinion "threatens the integrity of the securities markets." Pet. 22. The SEC, like "Turkey Lurkey"[10] in the "Chicken Little" folk tale, joins in the lament that the regulatory "sky is falling"; it argues that the Opinion could weaken its "ability to effectively police and deter insider trading," which could "undermine investor confidence in the fairness and integrity of the securities markets." SEC Amicus Br. 2. The SEC further suggests that the Opinion might lead to "confusion." SEC Amicus Br. 13.

These unsubstantiated concerns are highly exaggerated and unfair.[11] As the Opinion notes, the government historically has brought insider trading cases in

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[9] As Todd Newman points out in his Opposition to the Petition, the prosecution had full opportunity and incentive to introduce evidence of the defendants' knowledge of personal benefit at the trial. The government had rested its case before Judge Sullivan made his erroneous ruling that no proof of knowledge was required. Newman Opp'n Br. 9-10. This is not a case in which the government withheld offering evidence because it believed that the evidence was not required. The evidence of the defendants' knowledge of personal benefit was simply nonexistent.

[10] In the folk tale, "Turkey Lurkey" is a friend of Chicken Little who agrees to run with Chicken Little to tell the King that the sky is falling.

[11] They also ring hollow in light of public statements made by the government following the release of the Opinion. The United States Attorney's Office noted that the decision "affects only a subset of our recent cases." Press

circumstances in which corrupt tippers effectively sold inside information and the tippees knew of the corrupt conduct, usually because they participated in payoffs to the insiders. Opinion 14-15. Nothing in the Opinion jeopardizes the government's ability to bring such cases. It is only recently that the government has decided to push the doctrinal envelope, and bring cases in which tippers have not been charged with criminal acts and the defendants are remote tippees who are ignorant of the circumstances attending the tippers' disclosure of material nonpublic information. To the extent that convictions are jeopardized because the government cannot prove that the tippees knew that the tippers were receiving a personal benefit, *see, e.g.*, *United States* v. *Conradt*, No. 12 Cr. 887, 2015 WL 480419 (S.D.N.Y. Jan. 22, 2015) (cited at Pet. 24 n.5), the government is not in a position to complain. The Court has determined that such knowledge is required, and the government has explicitly decided not to contest this holding on rehearing. The government therefore must accept whatever consequences flow from the application of this principle of law.

Release, U.S. Attorney's Office for the Southern District of New York (Dec. 10, 2014), http://www.justice.gov/usao/nys/pressreleases/December14/StatementReNewmanChiasson2ndCir.php*; see also* Stephanie Russell-Kraft, *SEC's Ceresney Isn't Sweating 2nd Circ.'s Newman Ruling*, Law360 (Feb. 10, 2015, 6:10PM), http://www.law360.com/securities/articles/620472 ("Ceresney said the ruling shouldn't be a problem for the SEC, which has the 'ability to adapt' to the [decision]" and "his assessment of its potential impact was less gloomy than the SEC's recent argument in court").

The government's "sky is falling" argument also misreads and overstates the impact of the Opinion. For example, the Petition suggests that the Opinion would exempt from liability "a company executive's deliberate gift to a friend of information about an upcoming merger," with the result that tippee could earn millions because the tipper did not expect anything in return. Pet. 23 n.5. Putting aside the improbability that a jury would find no expectation of a *quid pro quo* on these facts, the Opinion would not be a bar to prosecution. As discussed *supra*, if the tipper disclosed the information for the purpose of permitting his friend to trade and reap profits, the tipping and trading would be illegal. The Opinion explicitly endorses this result. Opinion 22 (citing language in *United States* v. *Jiau* that liability may ensue if the relationship between the insider and the recipient "suggests . . . an intention to benefit the [latter].").

At another point, the government claims that the Opinion "invites selective leaking of valuable information to favored friends and associates of well-placed corporate insiders." Pet. 23. But, as indicated, if the insiders' relationship with the friends and associates involves the intention to permit them to trade and profit on the information, then this is tantamount to trading by the insiders and gifting the

proceeds to the "favored friends and associates." As the Opinion makes clear, Section 10(b) and Rule 10b-5 prohibit that conduct. Opinion 21-22.[12]

The government, in a final *cri de coeur*, suggests that the Opinion "provides a virtual roadmap for savvy hedge-fund managers and other traders to insulate themselves from tippee liability by knowingly placing themselves at the end of a chain of inside information and avoiding learning the details about the sources of obviously confidential and improperly disclosed information." Pet. 24. This suggestion fails in two respects. First, it completely ignores the "conscious avoidance" doctrine, which in appropriate circumstances treats intentional efforts to avoid culpable knowledge as the equivalent of knowledge. *See, e.g., United States* v. *Cuti*, 720 F.3d 453, 463 (2d Cir. 2013). Second, it betrays the government's continuing and obstinate refusal to come to terms with *Dirks'* personal benefit requirement. Information that is "obviously confidential," and even information that is "improperly disclosed," can be used to trade securities without committing insider trading fraud. The trading becomes fraudulent only if the insider discloses the information for personal benefit and the tippee knows this (or consciously avoids learning it). This is the law, and we respectfully suggest that the time has come for the government to accept it.

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[12] Even if the tipper did not disclose the information with the intent that the recipient trade on the information, the "selective leaking" by insiders to "favored friends and associates" would be prohibited by Regulation FD.

For better or worse, there is no indication that it intends to do so. In a Memorandum of Law filed shortly after the Panel decision in this case, the United States Attorney for the Southern District of New York took the position that there is no "personal benefit" requirement at all in cases brought under the misappropriation theory of insider trading. Gov't Mem. of Law in Supp. of the Sufficiency of the Defs.' Guilty Plea, *United States* v. *Durant*, 12 Cr. 887 (S.D.N.Y. Jan. 12, 2015). The government took this position despite having taken *precisely the opposite position in the briefing to the Panel in this case.* In this case, the government argued that, "for purposes of tippee liability, there is no material difference between a classical insider-trading case and a misappropriation case," Gov't Br. 55, and (citing *Obus*, *United States* v. *O'Hagen*, and *SEC* v. *Materia*) it insisted that personal benefit to the insider had to be shown in all such cases. Gov't Br. 54-55.[13] The Court agreed with this position, writing that "[t]he elements of tipping liability are the same, regardless of whether the tipper's duty arises under the 'classical' or the 'misappropriation' theory," Opinion 11, and including "personal benefit" to the insider as one of the required elements. Opinion 18. The ink was barely dry on the Court's opinion when the government executed its about-face. In the Memorandum of Law referenced above, the

[13] The government made this argument in service of its principal argument, now abandoned, that the tipper had to act for personal benefit in all cases, but in no case did a culpable tippee have to know this fact.

government opined at length about the doctrinal *differences* between classical theory and misappropriation theory cases, dismissed the language in the Panel opinion as *dicta* that had been issued "entirely *sua sponte*," and argued that "neither the Supreme Court nor the Second Circuit's precedents require proof of a personal benefit to the tipper . . . in misappropriation cases." Gov't Mem. of Law, *Durant*, at 5. Incredibly, in making this argument, the government relied on the same precedents it cited to this Court in this case to argue that personal benefit was a required element in misappropriation cases as well as classical theory cases.

We bring this stunning inconsistency to the Court's attention to make three points. *First*, in the event that the government's more recent analysis is correct, and there is no "personal benefit" requirement in misappropriation cases, then its "sky is falling" argument goes entirely by the wayside. The government brings most of its insider trading cases under the misappropriation theory. If "personal benefit" need not be proved in such cases, then the government's (and the SEC's) complaint that the Court has incorrectly "redefined" that element—meritless in any case—is beside the point in the lion's share of criminal and civil insider trading actions.

Second, the government's about-face reflects either its confusion about insider trading doctrine or, worse, its inclination to take whatever legal position serves its immediate interest in a particular case. At best, it illustrates that the

government's legal analysis about the subtleties of insider trading jurisprudence should be taken with a considerable grain of salt. The law as depicted in the brief that the government filed in this case—on a point with which this Court agreed—is now portrayed as something that is not the law and never was the law!

Third, this episode illustrates that courts, and undoubtedly this Court, will be speaking again to the scope of the insider trading prohibition. We believe that the Panel's decision was clear and correct in all respects, but if we are wrong then en banc reconsideration is nevertheless unnecessary. Another alternative, and in our view a better one, is to abide the event, and to consider these issues in a variety of cases and fact patterns as the case law continues to develop. As two wise commentators have written regarding the decision in this case, "[t]he Second Circuit's concern with the government's theory of prosecution is reminiscent of those occasions when the Supreme Court has called a halt to what it viewed as a misreading of a broad criminal statute and overzealous prosecution . . . . At these moments, the judicial and executive branches of government are speaking to one another . . . . Time will tell how the dialogue turns out on the scope of liability for insider trading." Elkan Abramowitz and Jonathan Sack, *Implications of Second Circuit Reversal Of Insider Trading Convictions*, N.Y. Law J., Jan. 6, 2015, at 3.

Finally, to the extent that the government and the SEC do sincerely believe that their enforcement agendas are threatened by the decision in this case, the SEC

can promulgate a regulation either implementing a different formulation of the "personal benefit" requirement or defining what constitutes fraudulent insider trading. Having failed for more than 50 years to issue a regulation that defines insider trading, it is remarkable that the agency now comes before this Court to complain about "confusion" in insider trading jurisprudence. If there is any "confusion," it results mainly from the SEC's refusal to use its authority to promulgate an appropriate regulation. It has been content instead to leave the job of defining insider trading to the courts, basking in the freedom to bring cases on a "we know fraud when we see it" basis. Having left to the courts the job of articulating the meaning of insider trading, the SEC should not now be heard to complain about "confusion" when it gets a result that it does not like.

CONCLUSION

The Petition for Rehearing should be denied.

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