



## Supreme Court finds that a family relationship is enough to establish the “tipper’s benefit” necessary to prove a charge of insider trading

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On December 6, 2016, the Supreme Court issued the awaited decision in *United States v. Salman*, partially rejecting a limited aspect of the Second Circuit’s landmark ruling in *United States v. Newman* regarding personal benefit in insider trading cases. Addressing the narrow question presented in *Salman*, the unanimous Supreme Court affirmed an insider trading conviction based on a family relationship between the tipper and tippee, overturning the Second Circuit to the extent that *Newman* required that a tipper also receive a tangible monetary benefit in exchange for a tip to a family member. However, the Court emphasized that the question of the sufficiency of personal benefit to a tipper is entirely dependent on the particular facts involved; a tip between two very close brothers was not a difficult question, but the decision leaves open the broader issue of defining the personal benefit required where there is no family relationship. In addition, *Salman* also does not address the requirement established by the Second Circuit in *Newman* that the downstream tippee must know that the original tipper received a personal benefit. So, while *Salman* makes clear that a family relationship is sufficient to infer the necessary “personal benefit” to the tipper, what constitutes a personal benefit in more attenuated or professional relationships remains an open question likely to be sorted out by the lower courts.

### The road from *Dirks* to *Newman* to *Salman*

Two years prior to *Salman*, on December 10, 2014, the Second Circuit issued its landmark ruling in *Newman*. The facts in *Newman* involved a trial court’s conviction of two downstream traders who received stock tips from analysts, who received the stock tips (both directly and indirectly) from corporate insiders. The evidence revealed that the traders were so removed from the earlier tips that neither remote tippee was aware of the original source of the stock tip—i.e., that it came from a corporate insider. The Second Circuit reversed the trial court, and in doing so rejected the government’s position that personal benefit to a tipper can be inferred solely from proof of a personal relationship between the tipper and his tippee; instead holding that an insider trading conviction requires proof of “a meaningfully close personal relationship that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature.” *United States v. Newman*, 773 F. 3d 438, 452 (2d Cir. 2014). The Second Circuit also held that a downstream tippee is only liable for insider trading if he or she knew that the

information came from corporate insiders who received a personal benefit in exchange for the information. The Supreme Court denied certiorari in *Newman* on October 5, 2015.

After the Second Circuit's decision in *Newman*, on July 6, 2015, the Ninth Circuit issued its opinion in *United States v. Salman*. 792 F.3d 1087 (9th Cir. 2015). *Salman* also involved the conviction of a downstream trader, although the involved tippers and tippees were all related. The tipper, a banker knowledgeable of information about corporate mergers and acquisitions (who is also the convicted trader's brother-in-law) gave tips on confidential deals to his brother, who passed the tip to their brother-in-law, Salman, who traded on the information. Judge Rakoff, of the Southern District of New York, sitting by designation and writing for the Ninth Circuit, affirmed the conviction and expressly declined to follow the Second Circuit's ruling in *Newman* that the tipper must have received a pecuniary or similarly valuable benefit in exchange for the tip. The Supreme Court granted certiorari on January 19, 2016, setting up the potential to resolve a perceived split between the Ninth and Second Circuits over what constitutes a personal benefit for insider trading purposes.

The unanimous Supreme Court affirmed the Ninth Circuit's decision, holding that a family relationship is sufficient to establish a personal benefit, where the tipper intended his tippee to receive the gift of valuable inside information. Justice Alito, writing the 8–0 opinion, relied on the Court's earlier ruling in *Dirks v. SEC*, a seminal opinion from 1983 on tipper liability for insider trading. Most importantly for this discussion, *Dirks* held that a tippee's liability is based on the tipper's breach of a fiduciary duty that occurs when the tipper discloses confidential information belonging to a third party, for a personal benefit. *Dirks* further had held that a "personal benefit" can be inferred by the jury or fact finder where the tipper gives the information to "a trading relative or friend."<sup>1</sup> (Slip Op. at 2 (quoting *Dirks v. SEC*, 463 U.S. 646, 664 (1983)).

Today, in *Salman*, the Supreme Court held that this holding from *Dirks* "easily resolves the narrow issue presented here," (Slip Op. at 8), because the *Salman* case involved a gift of information from an insider to his brother, a close relative. The Court rejected Salman's argument that *Newman* should apply to exonerate him, finding "[t]o the extent the Second Circuit held that the tipper must also receive something of a 'pecuniary or similarly valuable nature' in exchange for a gift to family or friends, we agree with the Ninth Circuit that this requirement is inconsistent with *Dirks*." (Slip Op. at 10 (quoting *Newman*, 773 F. 3d at 452)). The Supreme Court's explicit qualifier—"to family or friends"—underscores, in our view, the relatively limited scope of the ruling.<sup>1</sup>

Thus, while this decision is noteworthy and long-awaited, given its somewhat limited scope, federal circuit courts must be the guideposts in further developing what constitutes a "personal benefit" to tippers in cases that do not involve a close familial relationship, and when the defendant is a remote trader, removed by two or three different relationships from the initial tipper. For instance, if the next test case involves a tip between two professional acquaintances, and not two family members,

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<sup>1</sup> We reached that conclusion, in particular, due to the Supreme Court's discussion that "[t]he *Newman* defendants were several steps removed from the corporate insiders and the court found that there was no evidence that either was aware of the source of the inside information." (Slip Op. at 5) (internal quotations omitted). In contrast, here, the Court notes the very close family relationship between the tipper and his brother, and testimony that established that Salman received stock tips "from an extended family member, who received the information from Salman's brother-in-law." (Slip Op. at 2). Further, the evidence established that Salman knew the source of the inside information. (Slip Op. at 4-5). The juxtaposition of the two quite different fact patterns demonstrates the distinctions between *Newman* and *Salman*, and the limited scope and application of *Salman*'s holding.

and no money is exchanged, will a court extend the *Dirks* and *Salman* line of thinking? We suspect that *Salman* will apply, yet some courts may take a narrow interpretation of *Salman* and revert to something resembling a *Newman* analysis. Either way, we expect continued debate on these issues.<sup>2</sup>

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<sup>2</sup> For further background information on these matters, please see “*United States v. Newman*: Second Circuit clarifies its ‘Delphic’ interpretation of insider trading laws in landmark ruling,” available [here](#), as well as “First Circuit rejects Second Circuit’s higher standard for insider trading, finds the promise of a steak dinner sufficient to sustain a criminal conviction,” available [here](#).