Supreme Court has a chance to clarify insider trading

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Insider trading is a crime that can put a person away for more than a decade, and yet this crime exists nowhere in our federal statutes. It is a crime created by unelected judges, case by case, with each case differing slightly from the one that came before. On Wednesday the Supreme Court will hear argument in a case out of the Ninth Circuit, which held that the difference between insider trading and lawful trading might depend simply on the relationship between the people involved.

The case revolves around three men: two brothers and their brother-in-law, Bassam Salman. Maher Kara worked in Citigroup's healthcare investment banking group. He often discussed scientific concepts with his older brother, Mounir, who has a degree in chemistry. Mounir traded on some of the information he got from Maher and also passed this information along to Salman, who was then convicted of insider trading. Because Maher testified that he provided the information to Mounir to "benefit him" because he loved him, the Ninth Circuit found that Salman's use of the information he got from Mounir was criminal.

But in another recent case *U.S. v. Newman*, the Second Circuit found that no insider trading had occurred when non-public information was passed among mere acquaintances. No one passing along information received any sort of benefit in exchange for the information and therefore the trades did not constitute insider trading. But no benefit passed from Salman or Mounir to Maher in the Ninth Circuit case. What is the difference?

That is the question now before the Supreme Court: what does the person giving the information (the "tipper") have to get in exchange (from the "tippee") for the tippee's trades to be criminal?

At its most basic, insider trading occurs when someone uses a position of trust to gain information about a company and later trades on that company, without permission, to receive a personal benefit. The courts, in creating this crime, have relied on a section of the securities laws that prohibits the use of "any manipulative or deceptive device or contrivance" in connection with the purchase or sale of a security.

The courts' rationale has been that, by trading on information belonging to the company, and in violation of a position of trust, the trader has committed a fraud and earned "secret profits." The law, however, says nothing of "insiders" or "insider trading." And yet in 2015 alone the Securities and Exchange Commission (SEC) charged 87 individuals with "insider trading" violations.

The problem with the Salman case is that neither Mounir nor Salman gave anything to Maher in exchange for the information; Maher got no "secret profits." If Maher had traded on the information himself, he would almost certainly have been guilty of insider trading. Similarly, if Maher had given Mounir the information and said "I can't trade on this myself, so you trade instead and give me the money you make," that must fall within the definition of insider trading or else the prohibition would have no teeth. And if Maher had said "you trade on this information and use the profits to buy me a Ferrari" that would also count as insider trading; transforming the profits from cash to a valuable item still results in a personal benefit.

But there was no cash, no cars, nothing flowing into Maher's hands. Instead, the government has argued simply that because Maher loved his brother, the satisfaction he got from providing a benefit to his brother was enough. Since Salman should have known that the brothers had a close relationship, the court reasoned, he should have known that the information he received was ill-gotten.

In other words, even though both the information and the benefit flowed only from tipper to tippee, insider trading occurred. This is far from the *quid pro quo* arrangement usually required in these cases.

Some courts have found that it is enough if the tipper gives the information as a gift to the tippee. But there is a difference between an express gift – instead of a sweater, this Christmas I'm giving you a stock tip – and information provided out of a general feeling of benevolence toward an individual. The first is clearly defined and arguably relieves the tipper of purchasing a gift. The second makes any trade based on non-public information criminal, but *only* if the tipper loves the tippee.

The *Newman* case: no insider trading because they were all acquaintances. The *Salman* case: insider trading because they love each other. The result will certainly be courts inquiring into the relationships of tippers and tippees, trying to determine if they're close enough that the tipper got a "benefit" from giving away the information. The Ninth Circuit made much of Maher's love for Mounir and the closeness of the families. If they had loved each other less, would Salman still be facing prison?

People facing years in prison deserve better guidance than this. The Supreme Court has an opportunity to clarify these murky waters and make a felony turn on something less subjective and changeable than a man's feelings for his in-laws.

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