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White Collar Roundup - September 2012

This Is Crazy, but You Know My Number, so Tell Me Maybe

What is "material, nonpublic information" under the securities laws? The U.S. Court of Appeals for the Second Circuit discussed the meaning of that phrase in the context of an appeal after a conviction for insider trading. In the case, a tipper passed information about the acquisition of a publicly traded company to various tippees, including the defendant. At trial, the district court refused to include language in its definition of "material, nonpublic information" indicating that "general confirmation of an event that is 'fairly obvious' to knowledgeable investors is not material, nonpublic information." The court also said that "[t]he confirmation by an insider of unconfirmed facts or rumors--even if reported in a newspaper--may itself be inside information." The defendant claimed the court's refusal to give the first instruction and its giving of the second were errors. The Second Circuit disagreed. It reasoned that the court's charge "informed the jury that for information to be material it must be considered significant by reasonable investors. It conveyed to the jury that material, nonpublic information is information that either is not publicly available or is sufficiently more detailed and/or reliable than publicly available information to be deemed significant, in and of itself, by reasonable investors."

Just a Note About Forfeiture

In footnote 3 of that same opinion, the Second Circuit struck a blow to the U.S. Attorney's Office for the Southern District of New York's position of what property is forfeitable in insider-trading cases. That office applied 18 U.S.C. 981(a)(2)(A), which defines "proceeds" for "cases involving illegal goods, illegal services, unlawful activities, and telemarketing and health care fraud schemes" to be the entire amount obtained, without regard "to the net gain or profit realized from the offense." So, in practical effect the office required defendants to agree in any plea agreement in insider-trading cases to forfeit the entire value of the securities sold based on the tip, without taking into account the purchase price. The court rejected that interpretation and applied 18 U.S.C. 981(a)(2)(B), because although insider trading is illegal, trading in securities is a lawful activity. Subsection 981(a)(2)(B) applies to "cases involving lawful goods or lawful services that are sold or provided in an illegal manner" and defines "proceeds" as "the amount of money acquired through the illegal transactions resulting in the forfeiture, less the direct costs incurred in providing the goods or services." So, as the court explained, "the only money that should be subject to forfeiture in an insider trading case is money acquired when shares are traded based upon inside information at a gain. In cases where the securities are sold at a loss to avoid further losses, the direct costs associated with the sale, namely the cost of purchasing the securities sold, would exceed the 'money acquired' in the sale."

A Different Kind of "Substantial Assistance"

The Second Circuit concluded that to satisfy the "substantial assistance" requirement for aiding and abetting in a civil SEC enforcement action, the SEC must show that the defendant "in some sort associate[d] himself with the venture, that he participate[d] in it as in something that he wishe[d] to bring about, [and] that he [sought] by his action to make it succeed." The defendant in the case, who won his motion to dismiss in the district court, argued that "substantial assistance" should be defined as proximate cause. But the Second Circuit disagreed, noting that proximate cause "is the language of private tort actions; it derives from the need of a private plaintiff, seeking compensation, to show that his injury was proximately caused by the defendants' actions." The court noted that "in an enforcement action, civil or criminal, there is no requirement that the government prove injury," so proximate cause is irrelevant.

A Reprimand, a Reversal, a (Loaded) Question

In yet another blow to the Department of Justice,* the Second Circuit vacated the convictions in the "squawk box" case because of the prosecution's failure to turn over exculpatory evidence to the defense. The case was the second attempt at convicting the defendants for securities-fraud conspiracy for allegedly "front running" trades by conspiring with brokers to illegally listen to internal broadcasts of large trades in various securities. After the first trial resulted in a hung jury on the securities-fraud conspiracy, the government successfully retried that charge. After sentencing, the SEC initiated administrative proceedings against one of the defendants and in discovery produced various transcripts of investigative depositions that took place during the criminal investigation but that the government had not provided in discovery. Claiming these transcripts contained *Brady* material, the defendants moved for a new trial. The district court denied the motion, but the Second Circuit reversed. The Second Circuit also noted, "In light of the government's mishandling of material exculpatory and impeaching material, we wonder whether the government will choose to subject the defendants to yet a third trial."

*See also the *Stevens* case and the *Lindsay Manufacturing* case.

Die Hard With a Vengeance Indeed

The Ninth Circuit rejected the bid of famed *Die Hard* movie director John McTiernan to reverse the district court's refusal to suppress evidence. McTiernan had hired Anthony Pellicano to engage in illegal wiretapping on his behalf. During the government's investigation of Pellicano, an FBI special agent interviewed McTiernan about whether he had knowledge of Pellicano's wiretapping activities. McTiernan said he did not. But the FBI had a recording of McTiernan's conversation with Pellicano about wiretapping. McTiernan sought to suppress the audio recording after being charged with making a false statement to the FBI. The district court denied his motion. The Ninth Circuit held that Pellicano's use of wiretaps to memorialize the "to do list" for his private-investigation business was not a "criminal or tortious act," which would have warranted suppression under 18 U.S.C. 2511(2)(d), even though he was engaging in a criminal enterprise in his business. So, like Harry Ellis, McTiernan gambled and lost.

Full Boat: Aces Over Eights

Speaking of gambling, Eastern District of New York Judge Jack B. Weinstein ordered a Rule 29 judgment of acquittal in the case of Lawrence Dicristina, who had been found guilty by a jury for violating the Illegal Gambling Business Act (IGBA), which criminalizes certain gambling operations. No stranger to granting Rule 29 motions, Judge Weinstein detailed in his 120-page opinion the history of poker--the particular game at issue in Dicristina's case--which he concluded was more a game of skill than one of chance. Judge Weinstein concluded that both the government's view--that the IGBA criminalizes all gambling operations that are illegal under state law (New York state law criminalizes poker operations)--and Dicristina's view--that it only criminalizes gambling operations of games of chance that are illegal under state law--were plausible interpretations of the statute. Therefore, Judge Weinstein applied the rule of lenity and held that poker operations are not prohibited by the IGBA.

Defending His Honor

Southern District of New York Judge Jed Rakoff's position on his refusal to approve the consent judgment between the SEC and Citigroup Global Markets Inc. was argued to the Second Circuit by appointed pro bono counsel in this brief. In the appeal, the SEC and Citigroup both contend that Judge Rakoff abused his discretion in refusing to approve the consent judgment. In the U.S. District Court's brief, pro bono counsel argue both that the judge did not abuse his discretion and that the Second Circuit has no appellate jurisdiction. In one nugget from the brief, pro bono counsel contend that "[t]he SEC's and Citigroup's concept of deference--in which courts would be effectively reduced to potted plants--would surely undermine the independence of the federal judiciary."

"It Vexes Me. I'm Terribly Vexed."‡

The Hyde Amendment gives criminal defendants the chance to win attorney's fees and costs when "the court finds that the position of the United States was vexatious, frivolous, or in bad faith." After his acquittal in the Southern District of Florida, Ali Shaygan sought to recover his attorney's fees and costs under the Hyde Amendment. The district court granted him the award, noting that the prosecutors "acted vexatiously and in bad faith in prosecuting Dr. Shaygan for events occurring after the original indictment was filed and by knowingly and willfully disobeying the orders of this Court." On appeal, the Eleventh Circuit reverse, holding that even if a prosecutor had a subjective hostility toward the defendant, fees were not appropriate as long as the charge was not frivolous. The defendant has petitioned the Supreme Court to grant a writ of certiorari. In support of his petition, former federal judges, federal prosecutors and members of Congress filed a brief as *amici curiae*. In it, they argue that the Eleventh Circuit's holding "is a bolt from the blue" that "will disempower district judges, and send a clear signal that even grave prosecutorial misconduct will generally be overlooked, given the relatively lax standards for instituting federal prosecutions."

‡So said Commodus and, according to the district court, the prosecutors.