

Investors watch three  
key High Court cases

# Supreme Court Roundup



By Alla Zayenchik

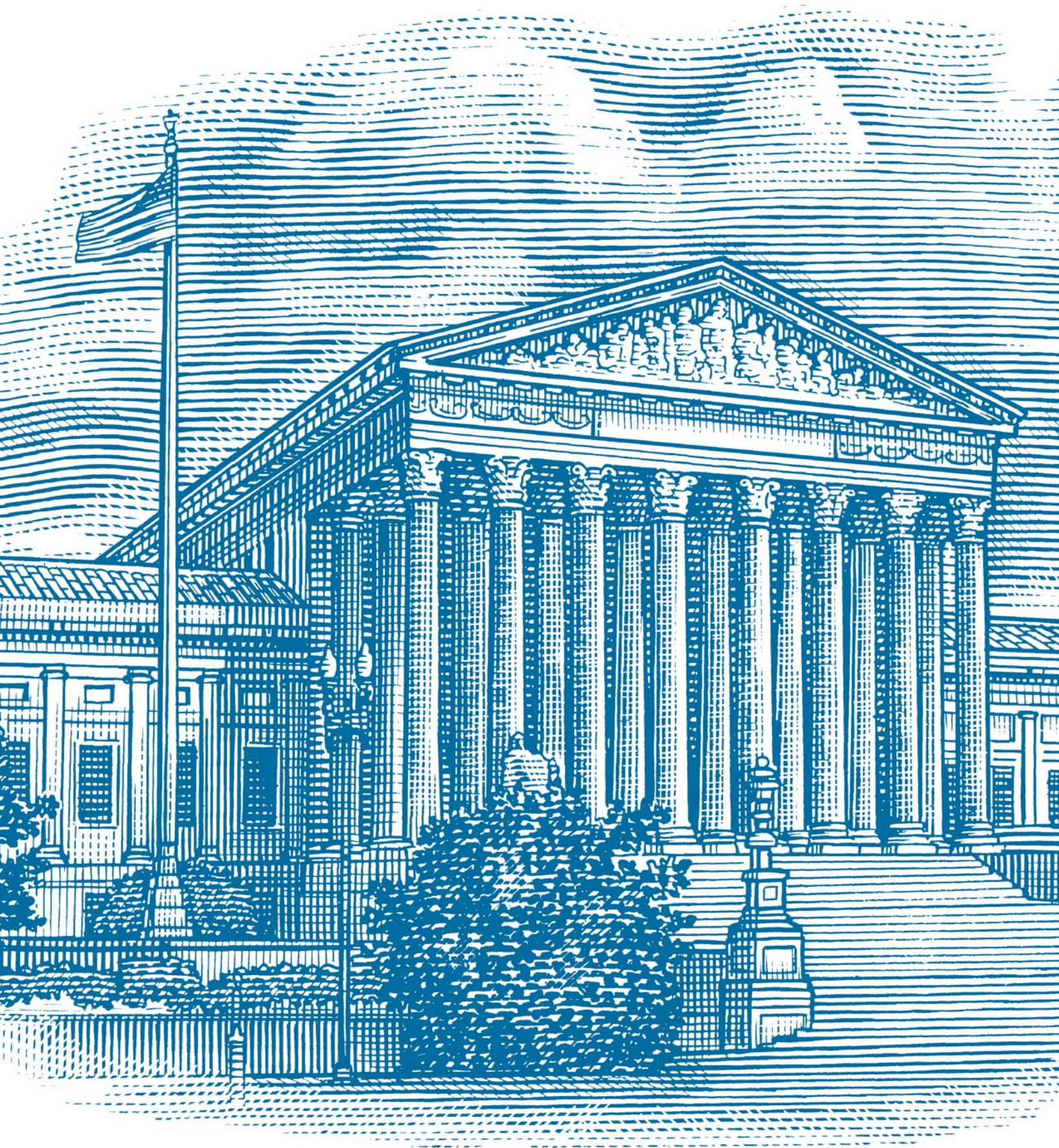
The Court's rulings continue to have a significant impact on securities cases and class action litigation.

**T**he Supreme Court's current roster has several cases of interest to the institutional investor community. These cases raise important issues, ranging from defendants' attempts to end a class action by buying off a representative plaintiff, to standards of liability for insider trading, to the possibility that the long-running Halliburton securities case may revisit the high court for the third time and continue to define the contours of liability under the general antifraud provision of the federal securities laws.

### **Supreme Court to Hear an Important Insider Trading Case**

Under the federal securities laws, it is forbidden to trade on the basis of material nonpublic information known only to company insiders. In *United States v. Newman*, 773 F.3d 438 (2nd Cir. 2014), the Second Circuit severely hindered the government's ability to prosecute insider trading cases when it held that in order to secure a conviction, prosecutors must prove that the receiving party knew that the insider shared material nonpublic information and also knew that the insider divulged the information to obtain a personal benefit in exchange for the tip. The practical implications of *Newman* are troubling, effectively destroying insider trading liability in all cases lacking a *quid pro quo*.







***The Supreme Court has agreed to hear an insider trading issue that resulted in a split between the Ninth and Second Circuits. The issue, which is of great practical consequence, is whether the government must prove that an individual who disclosed inside information did so in exchange for a personal benefit.***

In welcome news to the Department of Justice, the Supreme Court has agreed to hear *Salman v. United States*, an insider trading case that resulted in a split between the Ninth and Second Circuits. As in *Newman*, the issue at the heart of the *Salman* case is whether the government must prove, in order to secure a conviction, that an individual who disclosed inside information did so in exchange for a personal benefit. The defendant, Bassam Salman, was indicted for securities fraud and conspiracy to commit securities fraud arising from an insider-trading scheme involving members of his extended family. His brother-in-law Maher Kara, a member of Citigroup's healthcare investment banking group, had been providing information about upcoming mergers and acquisitions involving Citigroup clients to his brother Mounir "Michael" Kara.

Mr. Salman became close to the Kara family as a result of Maher's engagement to Salman's sister, and Michael shared with Mr. Salman the inside information provided to him by Maher, encouraging Salman to "mirror image" his trading activity. Salman booked trades through a brokerage account held by his wife's sister and her husband Karim Bayyouk. Salman, who was aware that the insider tips were coming from Maher, disclosed the information to Bayyouk and shared in the profits of Bayyouk's trading. As a result of the insider trading, Salman and Bayyouk's account skyrocketed from \$396,000 to over \$2 million.

Relying on *Newman*, Mr. Salman argued that prosecutors presented insufficient evidence that Maher disclosed the confidential information in exchange for a personal benefit or that Salman knew of the

benefit. Mr. Salman made this argument despite Maher's own testimony that he intended to "benefit" his brother and "fulfill" his needs. The Ninth Circuit rejected Salman's argument and sustained his conviction, finding that "the disclosure was intended as a gift of market-sensitive information," and that no evidence of a personal benefit to Maher was necessary. To hold otherwise, the Ninth Circuit reasoned, would yield a perverse result by allowing "a corporate insider or other person in possession of confidential and proprietary information [to] be free to disclose that information to her relatives, and they would be free to trade on it, provided only that she asked for no tangible compensation in return."

With the upcoming argument in the *Salman* case, the Supreme Court is expected to provide clarity as to whether an intention to benefit a family member, friend or acquaintance is sufficient to establish insider trading liability.

### **An Unaccepted Offer of Settlement Does Not Moot Class Claims**

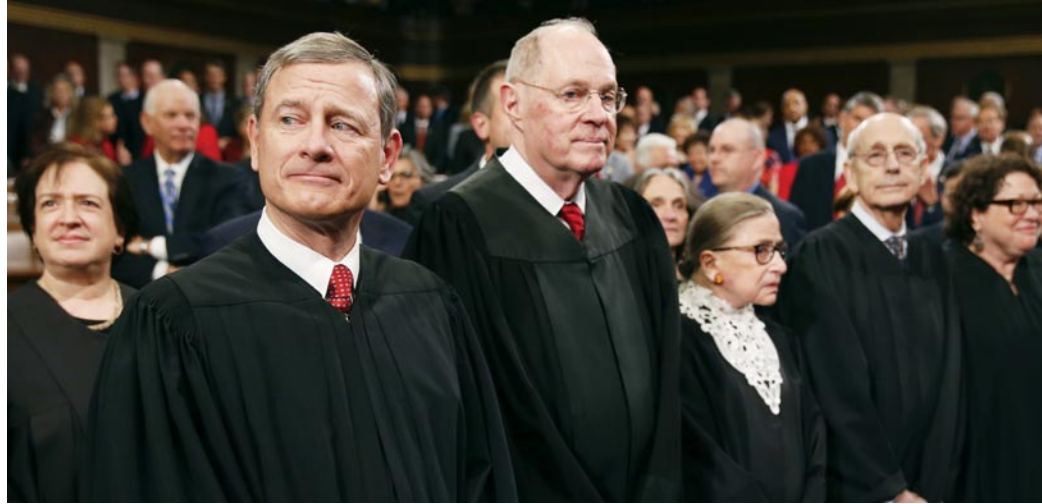
The Supreme Court recently addressed a question of significant practical import to class action litigation: whether a defendant's settlement offer under Rule 68 of the Federal Rules of Civil Procedure, providing complete relief to a representative or "named" plaintiff — but not to the rest of the plaintiff class — can moot the entire class action lawsuit.

In *Campbell-Ewald Co. v. Gomez*, the class consisted of individuals who received Navy recruiting text messages on their cell phones despite having not opted-in to receive such messages as required by

the Telephone Consumer Protection Act (“TCPA”). The named plaintiff, Jose Gomez, brought a class action lawsuit against the advertising agency that was sending these unsolicited text messages. Mr. Gomez sought \$500 in statutory damages for each violation of the TCPA, along with treble damages, injunctive relief, and an award of attorneys’ fees. Before the case was certified as a class action, Campbell made a Rule 68 offer to settle Mr. Gomez’s individual claims. Campbell did not, however, make a similar offer to settle the claims of the rest of the prospective class. After Mr. Gomez refused Campbell’s settlement offer, Campbell moved to dismiss under Rule 68.

The district court denied Campbell’s motion to dismiss, holding that the company could not “make an end-run around a class action simply by virtue of a facile procedural ‘gotcha,’ i.e., the conveyance of a Rule 68 offer of judgment to ‘pick off’ the named plaintiff prior to the filing of a class certification motion.” *Gomez v. Campbell-Ewald Co.*, 805 F. Supp. 2d 923, 930 (C.D. Cal. 2011). The Ninth Circuit affirmed the decision below and Campbell then appealed to the Supreme Court.

In January 2016, the Supreme Court upheld the Ninth Circuit’s opinion. Writing for the Court, Justice Ginsburg explained that “an unaccepted settlement offer has no force. Like other unaccepted contract offers, it creates no lasting right or obligation. With the offer off the table, and the defendant’s continuing denial of liability, adversity between the parties persists.” *Campbell*, 136 S. Ct at 667. The Supreme Court pointed out that a ruling in defendant’s favor would inappropriately “place the defendant in the driver’s seat” and



found that an unaccepted offer of settlement to the lead plaintiff cannot moot a class claim.

Justice Thomas authored a concurring opinion in which he agreed that an offer of complete relief does not moot a claim, but based the conclusion on common law principles rather than on Rule 68 or on contract law principles.

In contrast, Chief Justice Roberts issued a dissent suggesting that the majority’s decision was limited to its facts and that the outcome might have been different had the defendant actually deposited the funds with the district court. Chief Justice Robert’s dissent invites defendants to test the limits of the Court’s ruling in *Campbell* by attempting to “pick off” named plaintiffs via a payment that purports to provide “complete relief” to the named plaintiff only. Indeed, this very scenario was addressed by the Ninth Circuit in a case decided after *Campbell*. In *Chen, et al. v. Allstate Ins. Co.*, 2016 WL 1425869, at \*11 (9th Cir. April 12, 2016), the Ninth Circuit found that a putative class action was not moot where the defendant deposited the settlement offer funds in an

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***Halliburton II provided defendants with the opportunity to present evidence challenging whether alleged misrepresentations had an impact on a stock's price. Defendants argued that such evidence should be considered at the class certification stage, but the Court ruled that questions of materiality should be reserved for the merits stage. Defendants have appealed the issue and the Fifth Circuit has agreed to hear it.***

escrow account to be paid upon entry of judgment in plaintiff's favor. The Ninth Circuit reasoned that even though the money had been deposited into an escrow account, the plaintiff had not actually received the money and the defendant had the ability to reclaim the money if no judgment was entered. It remains to be seen whether courts outside the Ninth Circuit will adopt a similar view.

### ***"Halliburton III" on the Horizon?***

In November 2015, the Fifth Circuit agreed to hear the third appeal of the long-running securities class action, *Erica P. John Fund, Inc. v. Halliburton Co.* ("Halliburton"). Halliburton last visited the Supreme Court in 2014 ("Halliburton II") when the Court refused to overturn the presumption of class-wide reliance established in *Basic v. Levinson*, 485 US 224 (1988). In that appeal, the Court upheld the "fraud on the market" theory, a foundational principle of securities litigation, which holds that investors are entitled to rely on the integrity of the price of securities that trade on well-developed markets such as the New York Stock Exchange. However, the Court also afforded defendants an opportunity to rebut the presumption of reliance through a showing of direct or indirect evidence that an alleged misrepresentation did not have an impact on the stock price.

Applying the Supreme Court's ruling in *Halliburton II*, the trial court provided defendants with the opportunity to present evidence of lack of price impact. However, the judge determined that the evidence offered by the defendants was inadmissible at the class certification

stage. The defendants appealed, arguing that the court should have considered the evidence at class certification even though it went to the merits of the claim. As many commentators have noted, *Halliburton II* appears to be at odds with the Court's previous ruling in the *Amgen* case that questions of materiality — including lack of price impact — are not appropriately addressed at the class certification stage and should be reserved for the merits stage of the litigation process.

The Fifth Circuit agreed to hear the appeal in order to clarify what types of evidence can be presented at the class certification stage and what types of evidence must be reserved for later stages of the litigation. This appeal gives rise to the possibility that *Halliburton* will revisit the Supreme Court for a third time and require the Court to reconcile its opinions in *Halliburton II* and *Amgen*. If the arguments advanced by the defendants are accepted, it would increase the hurdles for investors to maintain securities fraud cases as class actions.

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