

CLIENT ALERT

Ineffective Insider Traders Avoid Double Whammy of a Failed Trade *and* Civil Penalties

June 14, 2011

The United States Securities and Exchange Commission's ("SEC") pursuit of insider traders was dealt a blow last week by the Second Circuit. The Second Circuit determined that the SEC may not pursue civil monetary penalties pursuant to § 21(d)(3) of the Securities Exchange Act of 1934,

15 U.S.C. § 78u(d)(3), against insider traders who neither profited nor avoided losses as a result of their illegal conduct. *SEC v. Rosenthal, et al.*, No. 10-1204 (2d Cir. June 9, 2011). The decision arose from a civil enforcement action by the SEC against a former law firm associate, Amir Rosenthal, and his brother and accountant, Ayal Rosenthal, for insider trading.

The crux of the case lay in the interpretation of two separate, yet interrelated, sections of the Securities Exchange Act of 1934: § 21(d)(3) and § 21(A). If § 21(A) were applied, the Rosenthal brothers would be subject to no civil penalty because under that statute the penalty is determined based on the amount of profit earned (or loss avoided). The SEC attempted to avoid that outcome by relying on § 21(d)(3) which permits a maximum penalty of \$120,000 per violation. The Second Circuit, while finding that the statutory language was ambiguous, rejected the SEC's efforts. "[I]t would be...absurd, to adopt the SEC's interpretation, which would permit a violator who made no profit to face a penalty up to \$120,000 per violation" pursuant to § 21(d)(3), while a violator who actually profited could be exposed to penalties of far less than \$120,000 pursuant to § 21(A).

As a result of the Second Circuit's decision, the SEC has one less weapon in its arsenal, at least when insider traders fail to benefit from their trades. Please do not hesitate to contact a member of the Crowell & Moring White Collar & Regulatory Enforcement practice group if you would like to discuss the implications of this ruling.

[Please click here to read the entire decision \[PDF\].](#)

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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