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THE RISE OF INSIDER TRADING AS A TITLE 18 OFFENSE

In this article, the authors introduce their subject by first tracing the evolution of the tangled 10b-5 insider trading law in the courts. They then turn to the growing practice of prosecutors to add the securities fraud provision in 18 U.S.C. §1348 to their charging instruments in insider trading cases. They close with the recent Blaszczak *case in which the Second Circuit declined to apply the "personal benefit" test to a Title 18 prosecution for insider trading.*

By Tom Hanusik, Rebecca Monck Ricigliano, and Nimi Aviad *

What is insider trading and when is it prohibited? A series of pivotal cases in the last six years, and scores of commentary, demonstrate that this seemingly straightforward concept, rooted in notions of fraud, is difficult to grasp. The culprit is the element of "personal benefit," which was grafted onto the crime by the Supreme Court almost 40 years ago, and has escaped clear definition since. Below we argue that the debates over the "personal benefit" standard, interesting as they are, may be sidelined by a prosecutorial trend which seeks to avoid the complicated Rule 10b-5 jurisprudence, and charges insider trading as securities fraud under Section 1348 of Title 18. A recent Second Circuit decision will no doubt propel this trend further, holding that the jurisprudential scaffolding added over the years to the crime of insider trading under Rule 10b-5 does not apply to Section 1348 cases.

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INSIDER TRADING LAW: A WORK IN PROGRESS

The Origins Story: Chiarella, Dirks, *and* O'Hagan

The current law of insider trading traces its origins to Section 10(b) of the 1934 Securities and Exchange Act, which broadly bans the use of any "manipulative or deceptive device" in connection with the purchase or sale of any security.[1] Section 10(b)'s purpose was clear: to promote the notion of market parity and allow parties to trade on the basis of the same publicly available information. However, congressional silence created a vacuum of interpretation with respect to specific

[1] 15 U.S.C. § 78j(b) (2012).

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violations, leaving the parameters of Section 10(b) to be explored through agency rulemaking and common law.[2]

To aid in enforcement of Section 10(b), the Securities and Exchange Commission crafted Rule 10b-5, making it unlawful for any person to "employ any device, scheme, or artifice to defraud," or to "engage in any act, [or] practice . . . which operates . . . as a fraud or deceit upon any person, in connection with the purchase or sale of any security."[3] Since the advent of modern insider trading law, the government has brought civil and criminal charges predominantly under Section 10(b) and Rule 10b-5.[4]

However, neither Section 10(b) nor Rule 10b-5 defines the crime of insider trading. These rules instead focus on vague prohibitions — fraud or deceit in connection with the purchase or sale of a security. Not surprisingly, insider trading jurisprudence is rife with ambiguity as a result. Early decisions established that corporate insiders had a fiduciary duty to others in the market to either abstain from trading or disclose all material nonpublic inside information ("MNPI") prior to trading.[5] The Supreme Court has taken the lead on driving the law forward, but the evolving standards of liability have been anything but clear.[6]

In *Chiarella v. U.S.*[7], a pillar of insider trading law, the Supreme Court addressed the extent of the duty to abstain or disclose. The Court focused on Chiarella's position as a corporate outsider (financial printer) in determining whether his silence before trading constituted a "manipulative or deceptive device."[8] Chiarella's position gave him access to redacted announcements of corporate takeover bids.[9] The Court reasoned that because Chiarella was not a corporate insider and owed no fiduciary duty, he did not have to abstain or disclose before trading.[10]

Chiarella made it clear that breach of a fiduciary duty was required for "insider" liability. However, the decision was unclear with regard to liability for downstream traders ("tippees") who traded on confidential information received from insiders ("tippers"), or their tippees, but owed no fiduciary duty to the source of the information.

Three years after *Chiarella*, the Supreme Court addressed this question in *Dirks v. SEC*.[11] Dirks received MNPI about a corporation's assets.[12] He conducted his own investigation and alerted other investors.[13] The Court affirmed the fiduciary duty theory of liability articulated in *Chiarella*, but recognized that a tippee knowingly trading on MNPI

[2] *Securities Exchange Act of 1934 – Insider Trading – Tippee Liability – Salman v. United States*, 131 HARV. L. REV. 383 (2017).

[3] 17 C.F.R. § 240.10b-5 (2017).

[4] Elkan Abrahamowitz & Jonathan S. Sack, *Back to the Future: Criminal Insider Trading Under Title 18*, N.Y.L.J (July 3, 2018).

[5] *Cady v. Roberts & Co*., 40 S.E.C. 907, 912 (1961) (finding liability based on the insider's access to information not intended for personal benefit and the inherent unfairness of a party taking advantage of information not available to others); *see also* Frank P. Luberti, Jr, *An Outsider Looks at Insider Trading* Chiarella, Dirks *and the Duty to Disclose Material NonPublic Information*, 12 Fordham Urb. L.J. 777 (1984) (discussing the development of the disclose or abstain rule).

[6] *United States v. Pinto-Thomaz*, 352 F. Supp. 3d 287, 295 (S.D.N.Y. 2018), *reconsideration denied*, No. S2 18-CR-579

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(JSR), 2019 WL 1460216 (S.D.N.Y. Jan. 10, 2019) (describing insider trading as a straightforward concept that courts have somehow managed to complicate).

[7] 445 U.S. 222 (1980).

[8] *Id.* at 226.

[9] *Id.* at 224.

[10] *Id.* at 230 (stating that silence in connection with the purchase or sale of securities may operate as a fraud but such liability is premised on a duty to disclose arising from a relationship of trust and confidence between parties to a transaction).

[11] 463 U.S. 646 (1983).

[12] *Id.* at 649.

[13] *Id.* at 650.

does not necessarily violate Rule 10b-5.[14] Indeed, the framework of insider trading law as articulated in *Chiarella* was not fashioned to find liability for downstream tippees lacking a fiduciary duty. To broaden liability, the *Dirks* Court crafted a rationale based on the derivative breach of the insider's fiduciary duty.[15] Liability required a breach of the insider's fiduciary duty and actual or constructive knowledge on the part of the tippee that the disclosure constituted a breach.[16] The insider's duty is breached when the insider "personally benefits, directly or indirectly," from the disclosure to the tippee.[17] Offering guidance to future litigants, the Court gave *examples* of objective scenarios resulting in personal benefits to the tipper: (1) pecuniary gains; (2) reputational benefits; (3) relationships suggesting a *quid pro quo* arrangement; and (4) gifts of confidential information to trading relatives or friends where the "[t]ip and trade resemble trading by the insider followed by a gift of profits to the recipient." [18] Under this framework, *Dirks* did not violate the law.[19]

After the government's loss in *Dirks*, it began developing a broader misappropriation theory to rope in traders who lacked a fiduciary duty, but whose conduct nevertheless generated the same concerns. Under this theory persons commit fraud "in connection with" a securities transaction, when they misappropriate confidential information, in breach of a duty owed to the source of the information.[20] The Supreme Court most notably applied this theory in *U.S. v. O'Hagan*.[21] O'Hagan, a law firm partner, became aware of an impending tender offer by virtue of his firm's representation of the acquiring company.[22] He traded in options ahead of the deal's public announcement and made a profit of $4.3 million.[23] Although O'Hagan owed no fiduciary duty to the firm's client, he violated his duty of loyalty and confidentiality to his firm and its client by taking and misusing the inside information.[24] The Court found this breach sufficient for liability.[25]

Both *Chiarella* and *O'Hagan* make clear that a breach of a duty to the source of the relevant information is a basis for insider trading liability. The convoluted *Dirks* decision and its "personal benefit" test served to extend liability down the chain, broadening the scope of potential liability under Section 10(b) and Rule 10b-5. While *Dirks* defined certain prohibited personal benefit scenarios, others, especially those not involving a pecuniary exchange, remained unclear.

The Personal benefit Test Strikes Back: Newman, Salman, *and* Martoma

The two-part test in *Dirks* attempted to describe when the actions of the tipper and tippee are so close that the insider's breach is imputed to the tippee.[26] But *Dirks*'*s* shaky directions left lower courts and practitioners scrambling to determine the exact parameters of the tippee-tipper relationship, including the limits of the personal benefit requirement.[27] Recognizing the difficulty in winning cases under *Dirks*, the government brought cases under the *O'Hagan* misappropriation theory and argued that *Dirks*'*s* personal benefit test did not apply.[28] Courts have oscillated on this point, however, with no clear consensus on whether proof of a personal benefit is required when proceeding under the misappropriation theory.[29]

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[14] *Id.* at 658-59.

[15] *Id.* at 659.

[16] *Id.* at 660.

[17] *Id.* at 662.

[18] *Id.* at 663-64.

[19] *Id.* at 665-67.

[20] *U.S. v. O'Hagan*, 521 U.S. 642, 652 (1997).

[21] 521 U.S. 642 (1997).

[22] *Id.*

[23] *Id.*

[24] *Id.* at 653.

[25] *Id.* at 650.

[26] *Id.* at 41.

[27] Adam C. Pritchard, Dirks *and the Genesis of Personal Benefit*, 68 S.M.U. L. REV., no. 3, 857 (2015); Donald C. Langevoort, *Informational Cronyism*, 69 STAN. L. REV. ONLINE 37, 42 (2016) (describing the pecuniary benefit prong of the personal benefit test as being satisfied not only by money, but also by trivial in-kind conveyances such as a jar of honey, dinners, and tickets to musicals).

[28] *U.S. v. Falcone*, 257 F.3d 226 (2d Cir. 2001); *see also* Langevoort, *supra* note 27, at 42 (describing the concerted move by the SEC and prosecutors to find liability based on the misappropriation theory due to the constraints posed by the two-part *Dirks* test.).

[29] Nelson S. Ebaugh, *Insider Trading Liability for Tippers and Tippees: A Call for the Consistent Application of the Personal Benefit Test*, 39 TEX. J. BUS. L. 265, 281 (2003); *see also SEC v. Willis*, 352 F. Supp. 3d 287 (S.D.N.Y. 1991) (holding that proof of personal benefit was not required under the

More than three decades after *Dirks*, the Second Circuit waded into the personal benefit waters and issued a decision drastically narrowing the concept of a personal benefit. In *U.S. v. Newman*,[30] a grand jury indicted two tippees for trading on MNPI disclosed by insiders. The tippees were several steps removed from the insiders and there was no evidence that either tippee knew the source of the MNPI.[31] The court considered whether the law required the government to prove the tippees' knowledge of the personal benefit to the insider.[32] Relying on *Dirks*, the Second Circuit found in the affirmative, holding that the government must establish the tippee's knowledge of the personal benefit to the tipper to demonstrate the tippee knew of the breach.[33] More notably, the *Newman* court held that in the context of gifts of information, not all relationships are alike. Under *Newman*, the inference of a personal benefit arising from a personal relationship between the tipper and the tippee was impermissible in the absence of 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."[34] The court therefore concluded that the government cannot prove the existence of a tipper's personal benefit "by the mere fact of a friendship, particularly of a casual or social nature."[35]

The court did not clarify how close the personal relationship needed to be to warrant an inference of personal benefit, but held that Newman's school- and church-based personal relationships on their own were not enough.[36] Thus, by suggesting that the personal benefit test was not automatically satisfied by a gift to a trading relative or friend, the Second Circuit placed *Newman* at odds with *Dirks*.

Newman turned insider trading law on its head, making it more difficult to prosecute tippees under both the classical-insider and misappropriation-outsider theories of liability.[37] *Newman* increased the government's burden when pursuing liability in the gift context by requiring an affirmative showing of a "meaningfully close personal relationship" without offering insight into the types of relationships that would meet the increased burden.[38]

Adding to the confusion, shortly after *Newman*, the Ninth Circuit reached an opposite conclusion.[39] In *Salman*, an insider provided tips to his brother, who then passed that information to Salman.[40] Salman argued that the government failed to produce evidence showing a pecuniary or reputational gain to the insider, of the quality that would establish a "meaningfully close personal relationship" under *Newman*. A mere family connection, Salman argued, was no longer enough to support liability.[41] The Ninth Circuit disagreed. Relying on *Dirks*, the court reiterated that the personal benefit requirement is met not only where the tipper receives a pecuniary or reputational gain, but also where "an insider makes a gift of confidential information to a trading relative or friend."[42]

Recognizing the circuit split created by *Salman* and *Newman*, the Supreme Court stepped in and affirmed the Ninth Circuit's decision.[43] The court unanimously held that the Ninth Circuit properly applied *Dirks*'*s* personal benefit test and that a personal benefit was present because the insider and initial tippee were brothers.[44] The Court affirmed that gifts of information to a trading relative or friend warrant an inference of personal benefit, even in the absence of tangible evidence of pecuniary or reputational gain.[45] Given that the Court decided the case by relying solely on *Dirks*, *Newman's*

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misappropriation theory); *but see SEC v. Yun*, 327 F.3d 1263, 1277-78 (11th Cir. 2003) (holding that the standard for tippers should be the same under either the classical theory or the misappropriation theory).

[30] 773 F.3d 438, 443 (2d Cir. 2014), *abrogated by Salman v. U.S.*, 137 S. Ct. 420, 429 (2016).

[31] *Id.*

[32] *Id.* at 447.

[33] *Id.* at 448.

[34] *Newman*, 773 F.3d at 452.

[35] *Id.*

[36] *Id.*

[37] Donna M. Nagy, *Beyond* Dirks*: Gratuitous Tipping and Insider Trading*, 42 J. CORP. L. 1, 5 (2016).

[38] *Securities Exchange Act of 1934 – Insider Trading – Tippee Liability – Salman v. United States*, 131 HARV. L. REV. 383, 384 (2017).

[39] *U.S. v. Salman*, 792 F.3d 1087 (9th Cir. 2015).

[40] *Id.* at 1089.

[41] *Id.* at 1093.

[42] *Id.*

[43] *Salman v. U.S.*, 137 S. Ct. 420, 429 (2016).

[44] *Id.* at 428.

[45] *Id.*

general requirement that the tipper and tippee share a "meaningfully close personal relationship" was not expressly overruled.[46]

The Second Circuit took the personal benefit test back to the drawing board in 2017, issuing two opinions in the same case.[47] In *U.S. v. Martoma*, a doctor with MNPI tipped Martoma who then traded on the information.[48] In its first opinion ("*Martoma I*"), the Second Circuit considered *Newman's* "meaningfully close personal relationship" requirement, and concluded that in light of the Supreme Court's *Salman* decision, the requirement no longer held.[49] In its second opinion ("*Martoma II*") — yet another indicator of the complexities of insider trading jurisprudence — the Second Circuit revived its "meaningfully close personal relationship" standard. Under *Martoma II*, a "meaningfully close personal relationship" required evidence of "a relationship between the insider and the recipient that suggests a *quid pro quo* from the recipient, or an intention to benefit the recipient."[50] Both the intention to benefit the tippee and a *quid pro quo* relationship allow for an inference of a meaningfully close personal relationship and therefore a personal benefit to the tipper.[51]

A NEW "HOPE": LIFTING THE SPECTER OF THE PERSONAL BENEFIT REQUIREMENT

While insider trading may be a "straightforward concept that some courts have managed to complicate,"[52] the original Supreme Court trilogy and the Second Circuit's shaky attempts to sort it out left a muddled doctrine and considerable doubt. As it now stands, criminal liability for insider trading under Rule 10b-5 depends on court-made definitions of "personal benefit," and on various degrees of friendship. Neither appears in the statute. As a result, traders — mostly tippees — cannot be certain whether their actions violate the current law. Prosecutors may struggle to frame and prove tipping-based insider trading cases. Defense counsel may need to guess just how strong the government's case truly is.

Against this backdrop, recent judicial holdings are circumventing altogether the "personal benefit" precondition grafted onto insider trading law in *Dirks*. In *Pinto-Thomaz*, for example, Judge Jed S. Rakoff explained that "insider trading is a variation of the species of fraud known as embezzlement," whereby someone to whom a company's material confidential information has been entrusted

> "secretly embezzles, or 'misappropriates,' the information in order to take advantage of its securities-related value. If the embezzler, instead of trading on the information himself, passes on the information to someone who knows it is misappropriated information but still intends to use it in connection with the purchase or sale of securities, that 'tippee' is likewise liable, just as any knowing receiver of stolen goods would be."[53]

It is therefore not the "personal benefit" to the tipper that matters, but rather whether the information was used to further a corporate (or otherwise permissible) purpose, or not.[54]

Similarly, faced with growing uncertainty for claims under Rule 10b-5 fueled by the Second Circuit's decisions in *Newman* and *Martoma*, prosecutors, especially in the district most affected by these rulings (the Southern District of New York), added securities fraud under Section 1348 of Title 18 to their charging instruments. This move harkens back to the heydays of insider trading enforcement. During the late 1980s, the Southern District often added Title 18 charges for mail and wire fraud to securities fraud charges under Rule 10b-5. At the time, prosecutors, uncertain whether the nascent "misappropriation" theory of insider trading would hold under a particular set of facts, leveraged fraud charges under Title 18 as a comfortable fallback

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46 *Id*.

47 *U.S. v. Martoma*, 869 F.3d 58 (2d Cir. 2017), *opinion amended and superseded by*, *U.S. v. Martoma*, 894 F.3d 64 (2d Cir. 2017); Benjamin Gruenstein and Miriam Rosenbaum, *Taking Insider Trading Too Far: What's Left of the 'Personal Benefit' Requirement after* U.S. v. Martoma*?*, N.Y.L.J. (July 23, 2019).

48 *U.S. v. Martoma*, 869 F.3d 58, 69 (2d Cir. 2017).

49 *Martoma*, 869 F.3d 58 at 69-70 (conviction affirmed, holding that an "insider or tipper personally benefits from a disclosure of inside information whenever the information is disclosed with the expectation that the tippee would trade on it, and the disclosure resembles trading by the insider followed by a gift of profits to the recipient, regardless of whether there was a meaningfully close personal relationship between the tipper and tippee") (internal quotation omitted).

50 *Id.*

51 *Id.*

52 *United States v. Pinto-Thomaz*, 352 F. Supp. 3d 287, 295 (S.D.N.Y. 2018), *reconsideration denied*, No. S2 18-CR-579 (JSR), 2019 WL 1460216 (S.D.N.Y. Jan. 10, 2019).

53 *Id.* at 296.

54 *Id.* at 298.

position. The move was largely abandoned after the misappropriation theory was endorsed by the Supreme Court's *O'Hagan* decision, as exhibited by a number of post-*O'Hagan* high-profile insider trading cases, which have not included Title 18 fraud charges of any kind.[55]

The reappearance of Title 18 fraud charges — this time around, of the securities fraud variety — is not anecdotal. For the purpose of this article, we surveyed insider trading charges brought by the Southern District of New York in 2017, 2018, and 2019. The survey showed significant Section 1348 charging activity. In 2017, three out of nine insider trading cases included charges under Section 1348 in addition to Rule 10b-5. In 2018, Section 1348 charges were added to one case (out of four); and in 2019, five cases out of a total of 10 saw parallel Rule 10b-5 and Section 1348 charges.

Securities Fraud under 18 U.S.C. § 1348

Much like Rule 10b-5, Section 1348 does not mention the term "insider trading." Enacted in 2002 as Section 807(a) of the Sarbanes-Oxley Act, Section 1348 broadly prohibits executing, or attempting to execute, "a scheme or artifice to defraud any person in connection with . . . any security of an issuer of a class of securities registered under Section 12 of the Securities Exchange Act of 1934."[56] This language mirrors the relevant enforcement sections of the mail, wire, and bank fraud statutes in Title 18.[57] A violation carries a prison sentence up to 25 years, which is higher than that for Title 15 securities fraud statutes.[58] Notably, Section 1348 is a criminal statute and therefore only the Department of Justice can use it to charge insider trading activity, as in the case for criminal charges under Rule 10b-5.[59]

Section 1348's legislative history indicates that Congress intended to "supplement the patchwork of existing technical securities law violations with a more general and less technical provision, with elements and intent requirements comparable to current bank and health care fraud statutes."[60] Senator Leahy noted that Section 1348 was needed because

> "there is no generally accessible statute that deals with the specific problem of securities fraud. In these cases, prosecutors are forced either to resort to a patchwork of technical Title 15 offenses and regulations, which may criminalize particular violations of securities law, or to treat the cases as generic mail or wire fraud cases, and to meet the technical elements of those statutes, with their five year maximum penalties."[61]

With Section 1348, Senator Leahy sought "needed enforcement flexibility and, in the context of publicly traded companies, protection against all the types [of] schemes and frauds which inventive criminals may devise in the future."[62]

Naturally, there has been far less precedent for the application and interpretation of Section 1348 than that of Rule 10b-5, and even less so in the insider trading context. The following elements have been used to instruct a jury on a Section 1348 charge in an insider trading case:

(1) the defendant executed a scheme to defraud a person to obtain money or property by materially false and fraudulent pretenses, representations, or promises;

(2) the defendant participated in the scheme knowingly, willfully, and with the intent to defraud; and

(3) the scheme to defraud was connected to the purchase or sale of stock in a company the securities of which were registered under Section 12 of the

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[55] *See, e.g.*, *U.S. v. Rajaratnam*, 719 F.3d 139 (2d Cir. 2013); *U.S. v. Goffer*, 721 F.3d 113 (2d Cir. 2013); *U.S. v. Gupta*, 747 F.3d 111 (2d Cir. 2014); *U.S. v. Steinberg*, 21 F. Supp. 3d 309 (2014); *U.S. v. Newman*, 773 F.3d 438, 443 (2d Cir. 2014), *abrogated by Salman v. U.S.*, 137 S. Ct. 420, 429 (2016); *U.S. v. Martoma*, 894 F.3d 64 (2d Cir. 2017).

[56] 18 U.S.C § 1348 (2009). Section 1348 also prohibits obtaining "by means of false or fraudulent pretenses, representations, or promises" any money or property from the purchase or sale of a security.

[57] 18 U.S.C. § 1341 (2008) (mail fraud); 18 U.S.C. § 1343 (2008) (fraud by wire, radio, or television).

[58] Prior to Sarbanes-Oxley, securities crimes prosecuted under Title 15 carried a statutory maximum of 10 years. Although Sarbanes-Oxley increased the Title 15 maximum to 20 years, section 1348 provides the longest potential jail term for people convicted of securities fraud.

[59] The SEC, therefore, does not have a similar outlet for civil or administrative insider trading enforcement actions.

[60] S. REP. NO. 107-146 (2002).

[61] *Id.*

[62] *Id.*

Securities Exchange Act of 1934, or was otherwise required to file reports under that Act.[63]

In *United States* v. *Blaszczak*, the trial judge instructed the jury that in the context of insider trading, a defendant has participated in a scheme to defraud if he participated in a scheme to embezzle or convert confidential information from the source by wrongfully taking that information and transferring it to his own use or the use of someone else.[64] Notably absent is the requirement that the insider received any kind of "personal benefit."

The Second Circuit's Decision in Blaszczak

In *Blaszczak,* the government charged four defendants with engaging in a scheme to convert confidential government property from the Centers for Medicare & Medicaid Services ("CMS") and trade on it. Specifically, Christopher Worrall, the "insider" who worked at CMS, shared "predecisional" information concerning CMS' contemplated rules and regulations with David Blaszczak, a "political intelligence" consultant for hedge funds. Blaszczak, in turn, shared that information with three partners, including Robert Olan and Theodore Huber, who worked at a healthcare-focused hedge fund. The latter three traded on the information. At trial, Judge Lewis Kaplan of the Southern District of New York instructed the jury that in order to convict the tipper (Worall) of Rule 10b-5 securities fraud, it needed to find that he tipped confidential CMS information in exchange for a personal benefit. Similarly, in order to convict the tippees (Blaszczak, Olan, and Huber) of Rule 10b-5 securities fraud, the jury needed to find that they knew the tipper disclosed the information in exchange for a personal benefit.

The defendants requested that the court include *Dirks*'s personal benefit test in its charge for the Title 18 wire fraud and securities fraud as well, but the district court refused. The Title 18 jury charge did not include any reference to the tipper's receipt of a personal benefit, or the tippees' knowledge thereof. As a likely result, the jury acquitted all defendants of insider trading under Rule 10b-5, but the traders Olan and Huber and the middleman Blaszczak were found guilty of insider trading under Section 1348.[65] In other words, even though the charges related to the same conduct, the jury voted to convict on securities fraud only under Section 1348 and not under Rule 10b-5.

The defendants appealed, arguing that the elements of insider trading should be the same across all statutes. *Blaszczak* therefore allowed the Second Circuit to decide, for the first time on the circuit level, whether standards or elements from Rule 10b-5's insider trading jurisprudence should be applied to Section 1348 insider trading charges.

The Second Circuit declined to implant Section 1348 with 40 years of Rule 10b-5 insider trading jurisprudence. Writing for the majority, Judge Richard J. Sullivan began by noting what both provisions have in common: "their text does not mention a 'personal benefit' test." Rather, both prohibit, with certain variations, "schemes to defraud."[66] These schemes, in turn, both encompass the so-called "embezzlement" or "misappropriation" theory of fraud, which proscribes the fraudulent appropriation to one's own use of the money

[63] Transcript of Trial Proceeding at 3972, *U.S. v. Blaszczak et. al*, No. 18-2811, 2019 WL 7289753, at *8 (2d Cir. Dec. 30, 2019). Interestingly, in an October 2018 article, Sandra Moser, then Acting Chief of the Fraud Section in the Department of Justice and Justin Weitz, Assistant Chief of the Fraud Section's Securities & Financial Fraud Unit, argued that conviction under Section 1348(1) does not require affirmative misrepresentations or material omissions and that the *mens rea* required to prove a violation of section 1348(1) is lower than a criminal violation of 10b-5 because it does not require proof of "willfulness." Sandra Moser & Justin Weitz, *18 U.S.C. § 1348 – A Workhorse Statute for Prosecutors*, 66 DEPT. OF JUSTICE J.FED. L. & PRAC. 111, 115, 121 (2018).

[64] Transcript of Trial Proceeding at 3973, *U.S. v. Blaszczak et. al*, *supra* note 63.

[65] Various commentators have noted the striking difference between the Title 15 and Title 18 jury instructions in the *Blaszczak* case. *See, e.g.,* Karen E. Woody, *The New Insider Trading*, ARIZ. ST. L.J. (forthcoming) ("The jury instructions for Rule 10b-5 consisted of nearly 20 pages of transcript and required the jury to address 10 specific issues related to whether the defendants had a duty of trust and confidence to CMS, whether there was a personal benefit granted in the exchange of information and whether the tippees knew of that personal benefit. In short, if the jury answered 'no' to any of the questions related to the elements of Rule 10b-5, it would acquit the defendants on that charge. In contrast, the jury instructions related to § 1348 were more sparse, and consisted of only four pages of the transcript. The government only needed to show that there was a 'scheme or artifice to defraud,' intent to defraud, and a connection to the purchase or sale of a security.").

[66] *U.S. v. Blaszczak et. al*, *supra* note 63 at *8.

or goods entrusted to one's care by another.[67] But, while the two provisions share similar text and proscribe similar theories of fraud, those similarities "have little to do" with the personal benefit test, which is a judge-made doctrine premised on the Exchange Act's statutory purpose.[68] Once outside the Exchange Act's unique statutory goals, the Second Circuit held there is no additional requirement that an insider breach a duty to the owner of the property, let alone that he benefited personally. The embezzlement itself — which is always also fraud — is enough.[69]

Moving to policy, the Second Circuit acknowledged that Section 1348 was added to the criminal code in large part "to overcome the technical legal requirements of the Title 15 fraud provisions" and to give prosecutors "a different — and broader — enforcement mechanism to address securities fraud than what had been previously provided in the Title 15 fraud provisions."[70] Allowing the "personal benefit" morass to plague Section 1348 as well would defeat these policy goals, even if the result was to give the Department of Justice an easier path to a criminal insider trading conviction than its civil counterpart at the Securities and Exchange Commission, limited to the narrower Rule 10b-5 framework.[71]

CONCLUSION

With the Second Circuit's approval, prosecutors are expected to continue to charge insider trading under both Rule 10b-5 and Title 18, or even focus solely on Title 18 charges. As a result, individuals, including corporate and government insiders, and investment professionals, face criminal, but not civil liability for the exact same conduct. While the defendants in *Blaszczak* raised this and other policy concerns, the court reminded the parties that "Congress was certainly authorized to enact a broader securities fraud provision, and it is not the place of courts to check that decision on policy grounds."[72] It is unclear, however, whether Congress would expound on its intentions by enacting a designated, and exclusive anti-insider trading statute.[73] The *Blaszczak* defendants, in the meantime, petitioned the Second Circuit for rehearing. ■

67 *Id.*

68 *Id.*

69 *Id.* at *9.

70 *Id.*

71 *Id.*

72 *Id.*

73 On December 9, 2019, a bipartisan majority of the US House of Representatives passed the Insider Trading Prohibition Act, which explicitly codifies a ban on insider trading. The bill is one of several pieces of legislation initially proposed after *Newman*. The bill, as amended, reflects several Republican priorities, such as the inclusion of an explicit personal benefit test consistent with *Dirks*, but does not include a significant Republican priority that any statute passed by Congress be "the exclusive insider trading law of the land." As such, its chances of receiving support in the Senate are low. Press Release, Financial Services Committee Republicans, McHenry Amendment Accepted to Improve Insider Trading Bill, Protect Good Faith Traders (Dec. 5, 2019). *See also*, Lyle Roberts, *The Insider Trading Law Is Bad. Will Congress Make It Worse?.* WALL ST. J. (Jan. 9, 2020), https://www.wsj.com/articles/the-insider-trading-law-is-bad-will-congress-make-it-worse-11578614315.