

CLASSICAL INSIDER TRADING THEORY

PRIMARY INSIDERS

PERMANENT: DIRECTORS, OFFICERS, EMPLOYEES WITH ACCESS TO INFORMATION

TEMPORARY: *Dirks v SEC*, fn. 14 (CB p 970) ATTORNEYS, ACCOUNTANTS, BANKERS ETC

TIPPEES : *Dirks v SEC* - there must be a breach of the insider's fiduciary duty before the tippee inherits the duty to disclose or abstain. Whether disclosure is a breach of duty depends in large part on the personal benefit the insider receives as a result of the disclosure. Absent an improper purpose, there is no breach of duty to stockholders. And absent a breach by the insider, there is no derivative breach. A tippee assumes a fiduciary duty to the shareholders of a corporation not to trade on material nonpublic information only when the insider has breached his fiduciary duty to the shareholders by disclosing the information to the tippee and the tippee knows or should know that there has been a breach.

DISCLOSE (the material information) TO MARKET AS A WHOLE OR ABSTAIN FROM TRADING

MISAPPROPRIATION THEORY

FIDUCIARIES OF INFORMATION SOURCES

ADVISERS TO PROSPECTIVE TENDER OFFERORS (*O'Hagan*)

LENDERS IN SYNDICATED LOANS, HOLDERS OF DEBT SECURITIES WHERE CONFIDENTIALITY AGREEMENTS (*SEC v. Barclays Bank PLC and Steven J. Landzberg*¹, settled May 2007)

JOURNALISTS

FAMILY MEMBERS

¹<http://www.sec.gov/litigation/litreleases/2007/lr20132.htm>

NOTE that if an insider discloses material information to a recipient in the context of a fiduciary relationship (e.g. a director consults her attorney) the insider will not breach her duties in doing so. The recipient is not a tippee if there is no breach by the insider. However the fiduciary relationship which protects the insider from liability creates a new source of obligation on the recipient who becomes a misappropriator if she uses the information or discloses it, obtaining a personal benefit.

DISCLOSE (intent to trade) TO INFORMATION SOURCE OR ABSTAIN FROM TRADING (*O'Hagan*)

BUT: In *SEC v Rocklage* (1st Cir. 2006) the Court said that an announcement of an intention to pass information on after it was received did not prevent the acquisition of the information from being deceptive:

On December 31, 2001, Mr. Rocklage learned that one of the company's key drugs had failed its clinical trial. That afternoon, he phoned Mrs. Rocklage to discuss the trial results and he reached her while she was in a limousine. Before discussing the results with her, Mr. Rocklage made clear his intention that the results be kept confidential. He told her that she was not to react to what he was about to say, and he instructed her not to discuss the results in front of the limousine driver. She agreed. From the time that Mr. Rocklage joined Cubist in 1994, he had routinely communicated material, nonpublic information to his wife, and she had always kept the information confidential. Based on Mrs. Rocklage's agreement, and based on their prior history of sharing nonpublic information about the company and her keeping that information confidential, Mr. Rocklage had a reasonable expectation that she would not disclose the trial results to anyone. Based on his understanding that she would keep the information confidential, Mr. Rocklage informed his wife that the clinical trial had failed. Before the results were disclosed to her, Mrs. Rocklage understood her husband's expectation of confidentiality....Unbeknownst to her husband, Mrs. Rocklage had a preexisting understanding with her brother, defendant Beaver, that she would inform him with "a wink and a nod" if she learned significant negative news about Cubist. At the time that Mrs. Rocklage learned the negative trial results, she knew or had reason to believe that Beaver owned Cubist stock. She also knew or had reason to know her brother would trade in Cubist securities if she disclosed the nonpublic information to him...

After that conversation, and on or about the evening of December 31, 2001, Mrs. Rocklage informed her husband that she planned to signal her brother to sell his stock. Mr. Rocklage urged her not to do so, and he expressed his displeasure at the idea. Nevertheless, sometime before the morning of January 2, 2002, Mrs. Rocklage called Beaver and gave him "a wink and a nod" regarding Cubist....

In light of her disclosure to her husband, Mrs. Rocklage's mechanism for "distributing" the information to her brother may or may not have been rendered non-deceptive by her stated intention to tip. But because of the way in which Mrs. Rocklage first acquired this information, her overall scheme was still deceptive: it had as part of it at least one deceptive device. Thus as a matter of the facts alleged in the complaint, and taking all facts and inferences in favor of the plaintiff, a § 10(b) claim is stated.

The defendants (the wife, her brother, and the brother's friend) agreed to settle the charges.