Debevoise & Plimpton

October 2018
Volume 4

INSIDER TRADING & DISCLOSURE UPDATE

In this Issue:

Editors' Remarks 01

Case Law & Market Updates

Cyan, Inc. v. Beaver Cty. Employees Ret. Fund: Supreme Court's Decision Raises Spectre of More Item 303 Disclosure Claims in State Court 01

SEC Spotlight on Cybersecurity 07

United States v. Martoma: Second Circuit Declines Rehearing in Case Analyzing *Salman's* Scope 09

SEC Enforcement Co-Director Emphasizes Nonmonetary Relief in SEC Actions 12

Update on *Morrison*: Building Section 10(b)'s Border Wall 13

Lucia v. SEC: Supreme Court Rejects Constitutionality of SEC ALJs 15

SEC Adopts Amendments to Simplify and Update Disclosure Requirements 17

Notes 21

Editors' Remarks

Welcome to the latest issue of the Insider Trading & Disclosure Update, Debevoise's periodic update focusing on recent legal, compliance and enforcement developments in the areas of insider trading, the management of material nonpublic information and disclosure-based matters.

In this Update, we highlight the potentially significant implications that the Supreme Court's *Cyan* decision could have on securities fraud class actions brought under the Securities Act of 1933. Also figuring prominently in this Update is the SEC's continuing focus on cybersecurity and a review of the continuing fallout from the Supreme Court's decision in the *Salman* insider trading case.

We hope that you find this Update useful and informative, and we look forward to bringing you further news and analyses in future issues.

Sincerely,

The Editorial Board

Case Law & Market Updates

Cyan, Inc. v. Beaver Cty. Employees Ret. Fund: Supreme Court's Decision Raises Spectre of More Item 303 Disclosure Claims in State Court

In one of the most significant securities-related decisions of the last term, the U.S. Supreme Court in *Cyan Inc. v. Beaver County Employees Retirement Fund* held that state courts have jurisdiction over class actions alleging violations of only the Securities Act of 1933 (the "1933 Act") and that defendants are not permitted to remove such actions to federal court.[1] The *Cyan* decision resolved a split among federal and state courts over whether the Securities Litigation Uniform Standards Act ("SLUSA") deprived state courts of jurisdiction over class actions asserting 1933 Act claims. While it is too early

Continued on page 2

***Cyan, Inc. v. Beaver Cty. Employees Ret. Fund*: Supreme Court's Decision Raises Spectre of More Item 303 Disclosure Claims in State Court**

Continued from page 1

to assess the full ramifications of the *Cyan* decision, many commentators have noted that the decision will likely ignite a race to file 1933 Act claims in state courts. As plaintiffs turn to potentially more favorable state court venues, it also seems likely that the *Cyan* decision will embolden them to pursue claims premised on Item 303 of SEC Regulation S-K—a trend that was already evident in federal court litigation. With state courts wading into the complex area of disclosure liability, the question of whether plaintiffs can assert claims based on an omission theory for failing to disclose "known trends and uncertainties" under Item 303 will assume even greater significance for defendants.

Statutory Underpinnings of *Cyan*

In the wake of the 1929 stock market crash, Congress enacted two laws to promote honest practices in the securities markets: the 1933 Act and the Securities Exchange Act of 1934 (the "1934 Act").[2] Federal and state courts have traditionally shared jurisdiction over 1933 Act claims, but all suits brought under the 1934 Act fall within the exclusive jurisdiction of federal courts.[3] In 1995, the Private Securities Litigation Reform Act (the "PSLRA") amended both Acts in an effort to stymie perceived abuses of the class-action vehicle in securities litigation. The PSLRA included both substantive reforms, applicable in state and federal court alike, and procedural reforms, applicable only in federal court.[4] But rather than face the new tightened standards for pleading securities fraud class actions in federal court, plaintiffs began filing such claims in state court.[5] In response to this end-run around the legislation, Congress enacted SLUSA in 1998. SLUSA's amendments to the 1933 Act require certain "covered class actions" alleging state law securities claims to be heard and dismissed in federal court.[6] But federal and state courts had been split for years over whether covered class actions filed in state court that allege *only* 1933 Act claims also must be heard in federal court.

Supreme Court's *Cyan* Decision

Investors in Cyan, Inc., a telecommunications company, filed a class action in California state court after the corporation's stock declined in value.[7] Bringing claims only under the 1933 Act, the investors alleged that the corporation's offering documents contained material misrepresentations. They did not assert any claims based on state law.[8]

Cyan then moved to dismiss the complaint for lack of subject-matter jurisdiction, arguing that SLUSA stripped state courts of power to adjudicate 1933 Act claims in "covered class actions."[9] The investors, in turn, argued that SLUSA left intact state courts' jurisdiction over all suits—including "covered class actions"—alleging only 1933 Act claims.

Continued on page 3

***Cyan, Inc. v. Beaver Cty. Employees Ret. Fund*: Supreme Court's Decision Raises Spectre of More Item 303 Disclosure Claims in State Court**

Continued from page 2

Siding with the investors, the California Superior Court refused to dismiss the case, and the California Court of Appeals denied review of this decision. The Supreme Court subsequently granted the corporation's petition for certiorari.[10]

In a unanimous opinion authored by Justice Elena Kagan, the Supreme Court held that "SLUSA did nothing to strip state courts of their long-standing jurisdiction to adjudicate class actions alleging only 1933 Act violations."[11] The Court explained that the background rule of § 77v(a) gives state courts concurrent jurisdiction over all suits "brought to enforce any liability or duty created by" that statute. Section 77p, which bars certain securities class actions based on state law, controls if there is a conflict between § 77v(a) and § 77p, but § 77p does nothing to limit state court jurisdiction over class actions brought under the 1933 Act, as it "says nothing, and so does nothing, to deprive state courts of jurisdiction over class actions based on *federal* law."[12] The Court explained that both the text and context of the statute supported its reading of the provision.

Under SLUSA, covered securities class actions based on the 1934 Act must still proceed in federal court.[13] Therefore, plaintiffs bringing claims pursuant to Section 10(b) of the 1934 Act, in tandem with Section 10 and 11 claims under the 1933 Act, must bring suit in federal court. Whether brought in state or federal court, the Supreme Court emphasized, the substantive protections of the PSLRA (such as the safe harbor for forward-looking statements) apply to all claims under both the 1933 and 1934 Acts.[14]

Finally, the Court answered a question raised by the federal government as *amicus curiae*: whether SLUSA enabled defendants to remove 1933 Act class actions from state to federal court for adjudication.[15] The government argued that § 77p(c) allowed defendants to remove 1933 Act class actions to federal court so long as they alleged the kinds of misconduct listed in § 77p(b).[16] But the Court found that the most natural reading of § 77p(c) actually refuted the government's view.[17] For this reason, the Court held that SLUSA did not permit defendants to remove class actions alleging only 1933 Act claims from state to federal court.[18]

Consequences of *Cyan*

Plaintiffs may now strategically bring 1933 Act claims against issuers, officers, directors, underwriters and others involved in the securities offering process in state court, where they can circumvent some of the PSLRA's procedural restrictions and avail themselves of more plaintiff-friendly standards. The most significant procedural difference between federal and state court is the lack of a meaningful motion-to-dismiss process in state court. For example, in many state courts, such as in California, the pleading standard for falsity is vastly

Continued on page 4

***Cyan, Inc. v. Beaver Cty. Employees Ret. Fund*: Supreme Court's Decision Raises Spectre of More Item 303 Disclosure Claims in State Court**

Continued from page 3

lower than the particularity standard established by Federal Rule of Civil Procedure 9(b), requiring no more than notice pleading. This means that significantly fewer 1933 Act claims will be dismissed at the pleading stage. Moreover, state court judges may lack the expertise of their federal counterparts in handling complex 1933 Act claims.

Impacts on Claims Premised on Item 303 of Regulation S-K

The *Cyan* decision also may have a particular impact on the increasing number of 1933 Act claims premised on Item 303 of SEC Regulation S-K. Sections 11 and 12(a)(2) of the 1933 Act impose liability on certain participants in a registered securities offering when the registration statement or prospectus contains material misstatements or omissions.[19] Unlike Section 10(b) claims, claims under Sections 11 and 12(a)(2) under the 1933 Act do not require allegations of scienter, reliance or loss causation.[20]

Item 303 requires that companies describe in their annual and quarterly reports "any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations."[21] Disclosure under Item 303 is necessary "where a trend, demand, commitment, event or uncertainty is both presently known to management and reasonably likely to have material effects on the registrant's financial conditions or results of operations."[22] Notably, Item 303 requires the registrant to disclose only those trends, events or uncertainties that it *actually knows* of when it files the relevant report with the SEC; it is not enough that it *should have known* of the existing trend, event or uncertainty.[23] With respect to materiality, "the complaint may not properly be dismissed on the ground that the alleged misstatements or omissions are not material unless they are *so obviously unimportant to a reasonable investor* that reasonable minds could not differ on the question of their importance."[24]

Plaintiffs have increasingly brought Section 11 and 12(a)(2) claims under the 1933 Act based on Item 303 obligations in federal court with mixed results. In a recent Section 11 action filed in the U.S. District Court for the Southern District of New York, the plaintiffs alleged that the defendant was required to disclose under Item 303 the "significant deterioration of subprime and Alt-A credit market positions," which was known only to the defendant prior to the Series 5 offering.[25] But the court disagreed, finding that the defendant's disclosures satisfied Item 303.[26] Moreover, the court held that "[e]ven if [defendant] breached Item 303's disclosure duty, the omissions are still not actionable under Section 11 because they are immaterial."[27] In other recent cases, however, courts have upheld Section 11 and 12(a)(2) claims, finding

Continued on page 5

***Cyan, Inc. v. Beaver Cty. Employees Ret. Fund:* Supreme Court Confirms State Courts' Jurisdiction Over Class Actions for Securities Act of 1933 Violations**

Continued from page 4

that the defendants failed to meet their Item 303 obligations. In *Litwin v. Blackstone Grp.*, for example, the Second Circuit found that the plaintiffs had adequately pleaded that the defendant omitted material information that it was required to disclose under Item 303 of Regulation S-K.[28] The plaintiffs, the court explained, had "allege[d] that the downward trend in the real estate market was already known and existing at the time of the IPO, and that the trend or uncertainty in the market was reasonably likely to have a material impact on Blackstone's financial condition."[29] Likewise, in *Panther Partners Inc. v. Ikanos Commc'ns, Inc.*, a supplemental registration statement failed to mention a known "substantial" product design defect, which might cause returns and supplemental refunds, and instead generally cautioned that the products "frequently contain defect and bugs."[30] The Second Circuit concluded that the plaintiff had "adequately alleged that the disclosures concerning a problem of this magnitude were inadequate and failed to comply with Item 303."[31]

Cyan will likely lead plaintiffs alleging similar 1933 Act claims based on Item 303 to seek recourse in state court, where the PSLRA's procedural protections do not apply, and judges may have less experience with complex securities matters.

Future of 1934 Act Claims Based on Item 303 Remains Unclear

Whether or not shareholders can bring private actions for securities fraud under Section 10(b) premised on a corporation's failure to disclose information required by Item 303 remains an open issue. In March 2017, the U.S. Supreme Court granted certiorari in *Leidos, Inc., v. Indiana Public Retirement System* to resolve a split among the circuit courts as to whether the failure to make a disclosure required by Item 303 is an actionable omission under Section 10(b) of the 1934 Act.[32] Unfortunately, on October 17, 2017, as a result of a last-minute settlement, the Supreme Court announced that it would no longer resolve the closely watched conflict.[33]

The circuit split thus remains open. In two decisions, *Indiana Pub. Ret. Sys. v. SAIC* and *Stratte-McClure v. Morgan Stanley*, the Second Circuit has held that a failure to comply with Item 303 can give rise to liability under Section 10(b).[34] This approach directly conflicts with the Ninth Circuit's and Third Circuit's conclusions in *In re NVIDIA Corp. Securities Litigation* and *Oran v. Stafford*, respectively, that an Item 303 omission *cannot* support Section 10(b) liability.[35] Particularly in circuits where Item 303 violations *cannot* lead to Section 10(b) liability, plaintiffs may try to style such allegations under Sections 11 and 12(a)(2) and seek recourse in state court.

Continued on page 6

***Cyan, Inc. v. Beaver Cty. Employees Ret. Fund:* Supreme Court Confirms State Courts' Jurisdiction Over Class Actions for Securities Act of 1933 Violations**

Continued from page 5

Key Takeaways

Plaintiffs filing 1933 Act claims may now take advantage of state courts perceived to be friendlier to their interests. *Cyan* will have the most significant impact in states where courts previously interpreted SLUSA to afford exclusive federal court jurisdiction—or at least the removability—of 1933 Act claims. Moreover, *Cyan* will heighten the odds that defendants face litigation in multiple forums in 1933 Act cases, as plaintiffs can now freely file in state and/or federal court. As a practical matter, *Cyan* will increase the overall number of unconsolidated securities class actions. Given that state court securities class actions cannot be removed, related securities class actions likely cannot now be consolidated in a single forum, undermining the objectives underlying the PSLRA's consolidation and lead-plaintiff appointment process.

Parallel state and federal class actions may also result in weakened procedural protections in the related federal case. In particular, state courts may refuse to stay discovery while a motion to dismiss is pending on the grounds that the PSLRA's automatic discovery stay applies solely in federal court. As a result, defendants may be less able to protect themselves against abusive lawsuits and the burdensome discovery costs that the PSLRA sought to rein in.

Furthermore, an individual and nominal investor, whose interests may not align with those of the class, can now file a Section 11 class action in state court related to the Section 10(b) class action proceeding in federal court. This could deprive the "most adequate plaintiff" in federal court of strategic control over the litigation, undercutting a settlement that is in the class's best interests.

Issuers should carefully scrutinize their disclosures given the potential for increased litigation exposure following *Cyan*. In addition, public companies and their defense counsel may need to adjust their litigation strategies to effectively handle the complicated risks engendered by *Cyan*. In particular, counsel should be prepared to quickly understand the procedural rules of state courts and should take steps to coordinate responses to parallel litigations in federal and state courts.

Finally, it is reasonably possible that the increased securities class action filings in state court and the increased cost and inconsistent outcomes resulting from an increase in unconsolidated class actions may some day prompt Congress to enact new legislation—along the lines of SLUSA—to ensure that plaintiffs bring particular securities class actions only in federal court.

SEC Spotlight on Cybersecurity

On October 16, 2018, the U.S. Securities and Exchange Commission (the "SEC") issued a Report of Investigation (the "October Report") urging issuers to evaluate their systems of internal accounting controls in light of the current risk environment, including emerging cyber risks.[1] The October Report was issued in connection with an investigation by the SEC's Division of Enforcement, in consultation with the Division of Corporation Finance and Office of the Chief Accountant, into whether nine public issuers violated federal securities law requirements regarding internal accounting controls after they each lost millions of dollars, in one case with losses exceeding $45 million, due to cyber frauds perpetrated through spoofed or manipulated electronic communications. Although the SEC ultimately determined not to pursue any enforcement action, the October Report underscores the need for issuers to devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions are executed with, or that access to company assets is permitted only with, management's general or specific authorization. The October Report is yet another example of the SEC's continued focus on cybersecurity issues, building upon the SEC's February 2018 cyber guidance.

In February 2018, the SEC issued interpretive guidance to assist public companies in preparing disclosures about cybersecurity risks and incidents.[2] Although similar in many ways to previously issued SEC guidance from 2011,[3] the 2018 guidance addressed two additional topics. First, the SEC emphasized the importance of companies maintaining "appropriate and effective disclosure controls and procedures to enable them to make accurate and timely disclosure of material events, including those related to cybersecurity."[4] Second, the SEC included a new cautionary note that "directors, officers, and other corporate insiders must not trade a public company's securities while in possession of material nonpublic information, which may include knowledge regarding a significant cybersecurity incident experienced by the company."[5] The SEC has since taken enforcement action based upon these aspects of the February guidance, turning its attention to cyber-related internal controls, disclosure practices and insider trading violations.

In April 2018, the SEC announced that Altaba, formerly known as Yahoo! Inc., had agreed to pay $35 million to settle charges that it misled investors when it failed to properly investigate, evaluate and disclose a massive data breach of millions of users' personal data.[6] The SEC order found that Yahoo "failed to maintain disclosure controls and procedures designed to ensure that reports from Yahoo's information

Continued on page 8

SEC Spotlight on Cybersecurity

Continued from page 7

security team concerning cyber breaches, or the risk of such breaches, were properly and timely assessed for potential disclosure."[7] While noting that the SEC defers to "good faith exercises of judgment about cyber-incident disclosure," Steven Peikin, Co-Director of the SEC Enforcement Division, stated that Yahoo's response was "so lacking that an enforcement action [was] warranted."[8]

The SEC's focus on internal controls to protect against cyber frauds has extended beyond issuers to other market participants as well. In September 2018, the SEC announced that Voya Financial Advisors Inc., a Des Moines-based broker-dealer and investment advisor, had agreed to pay $1 million to settle charges relating to violations of the Safeguards Rule and the Identity Theft Red Flags Rule.[9] The SEC's order states that cyber intruders were able gain access to personal information of over 5,000 customers and that weaknesses in Voya's cybersecurity procedures led to both the intrusion itself and the failure of Voya to terminate the intruders access in a timely manner.[10] Robert A. Cohen, Chief of the SEC Enforcement Division's Cyber Unit, stated, "This case is a reminder to brokers and investment advisers that cybersecurity procedures must be reasonably designed to fit their specific business models."

Following this action, in a speech at Georgia State University College of Law, SEC Commissioner Kara Stein advocated for the expansion of an SEC rule, Regulation Systems Compliance and Integrity, which seeks to improve market infrastructure resiliency by requiring certain market participants "to establish written policies and procedures reasonably designed to ensure that their computer systems can maintain their operational capability in the event of a disruption."[11] Commissioner Stein argued that it should cover other "key market players…such as broker-dealers, investment advisors and transfer agents" and that everyone must "up their game to protect our critical systems, personal data and economy from cyber threats," a message echoed in the October Report.[12]

SEC enforcement has also trained its eye on cyber-related insider trading violations. In March and June 2018, the SEC charged former Equifax executives with trading on inside information concerning the company's 2017 data breach prior to Equifax's public disclosure of the breach.[13] Although the Equifax breach was particularly high profile and the allegations egregious, the SEC has publicly stated that it is proactively collecting and reviewing public and nonpublic data and then tracking trading activity to identify suspicious transactions.[14]

The October Report, as well as the enforcement actions focused on cyber issues, serve as good reminders to SEC reporting companies to review all of their controls, policies and procedures against the current cyber-threat environment.

United States v. Martoma: Second Circuit Declines Rehearing in Case Analyzing *Salman's* Scope

Following the Supreme Court's 2016 decision in *Salman v. United States*,[1] federal courts have grappled with the decision's ambiguities and, in particular, its impact on the Second Circuit's 2014 opinion in *United States v. Newman*.[2] Perhaps no decision more clearly exemplifies the challenges courts confront in attempting to interpret and apply *Salman* than the Second Circuit's recent decisions in the *United States v. Martoma*[3] case, in which former SAC Capital portfolio manager Mathew Martoma appealed his conviction for securities fraud, in connection with an insider trading scheme, to the very court that had authored *Newman*.

Background

The Supreme Court in *Salman* partially resolved a debate among the lower courts—the circumstances under which a person who tips inside information personally benefits from the tip and thus breaches a duty—by abrogating the Second Circuit's 2014 opinion in *United States v. Newman*.[4] The Supreme Court did not state with precision, however, how much of *Newman*'s holding it had abrogated and whether *Newman*'s controversial interpretation of the seminal insider trading case *Dirks v. Securities and Exchange Commission* survived.[5] *Newman* elaborated on the gifting theory of personal benefit, holding that such a benefit required evidence of a "meaningfully close personal relationship" between tipper and tippee "that generates an exchange that is objective, consequential, and represents at least a potential gain of a pecuniary or similarly valuable nature."[6] Adhering closely to *Dirks*, the Court's *Salman* opinion invalidated *Newman* "[t]o the extent the Second Circuit held that the tipper must … receive something of a pecuniary or similarly valuable nature in exchange for a gift to family or friends"[7]—language that did not expressly overturn *Newman*'s "meaningfully close personal relationship" standard and passed to lower courts the job of elucidating *Salman*'s impact on Second Circuit precedent.

Martoma's Appeal

Martoma, whose conviction had predated *Newman* by several months, challenged the trial court's jury instructions for having omitted *Newman*'s "meaningfully close personal relationship" language. Martoma's argument necessarily assumed that the "meaningfully close personal benefit" portion of *Newman*'s holding had survived the Supreme Court's analysis in *Salman*. In its initial opinion, issued in August 2017, a divided Second Circuit panel affirmed Martoma's

Continued on page 10

***United States v. Martoma*: Second Circuit Declines Rehearing in Case Analyzing *Salman's* Scope**

Continued from page 9

securities fraud conviction and seized the opportunity to revisit the circuit's precedent. Although the majority acknowledged that *Dirks* and *Salman* had focused on gifts to "relatives and friends," they assessed that "the straightforward logic of the gift-giving analysis in *Dirks*, strongly reaffirmed in *Salman*, is that a corporate insider personally benefits whenever he discloses inside information as a gift . . . with the expectation that the recipient would . . . exploit it for his pecuniary gain."[8] By way of example, the majority suggested that a corporate insider should be liable for providing his doorman with inside information, in place of actual cash, as a holiday gift. "[T]he personal benefit one receives from giving a gift of inside information," the majority explained, "is *not* the friendship or loyalty or gratitude of the recipient of the gift; it is the imputed pecuniary benefit of having effectively profited from the trade oneself and given the proceeds as a cash gift."[9] The majority concluded that "the logic of *Salman*" abrogated *Newman*'s "meaningfully close personal relationship" requirement.[10]

A dramatic split among the panel raised questions as to whether the holding could survive *en banc* review, which Martoma promptly petitioned. In a dissent as lengthy as the majority opinion, Circuit Judge Rosemary Pooler cautioned that the decision "severely damage[d] the limitation provided by the personal benefit rule, and cast[] aside Circuit precedent and Supreme Court rulings to do so," by removing the "friend or relative" requirement from the otherwise "vague and subjective" concept of a "gift."[11] Pooler added that gifts to a friend or relative provide a tipper with direct benefits that do not arise from gifts to acquaintances or strangers—including obviating the need to give an expected loan, genuine enjoyment of the tippee's happiness, and improved relations with friends and relatives.[12] Outlining the history of the personal benefit standard, her dissent also argued that the Supreme Court had "explicitly considered but did not adopt" the majority's interpretation of the gifting rule.[13]

The Second Circuit Panel's Amended Opinion

In a strange turn of events, on June 25, 2018, while Martoma's petition for rehearing *en banc* was pending before the full Second Circuit, the divided panel revisited its decision. In an amended opinion, the majority again upheld Martoma's securities fraud convictions but dialed back its finding that *Salman* had abrogated *Newman*'s "meaningfully close personal relationship" holding. Instead, the majority allowed that the jury instructions were inconsistent with *Newman* but that, because "*Newman* cabined the gift theory using two other freestanding personal benefits that have long been recognized by our case law," the instructions' primary flaw was their failure to require either (1) a finding that the relationship suggested a *quid pro quo* or (2) a finding of an intention

Continued on page 11

United States v. Martoma: Second Circuit Declines Rehearing in Case Analyzing *Salman's* Scope

Continued from page 10

by the tipper to benefit the tippee.[14] In its analysis of *Newman*, the majority emphasized that an intention to benefit a tippee is a standalone personal benefit: "Whichever way *Dirks* is read, it recognizes that purposefully benefitting the tippee with inside information proves that the tipper has received a personal benefit in breach of fiduciary duty."[15] With respect to whether evidence of any particular relationship may be required for such a finding, the majority added, "We think it clear that the answer is no."[16] Citing evidence that at least one tipper had received $70,000 as a *quid pro quo* for his disclosure of confidential information and that another tipper intended to benefit Martoma, the majority found that the instructional errors were harmless. The majority's opinion concluded that "because there are many ways to establish a personal benefit, we . . . need not decide whether *Newman*'s gloss on the gift theory is inconsistent with *Salman*."[17]

Judge Pooler's revised dissenting opinion dismissed the majority's revisions as "semantic rather than substantial."[18] Calling out the majority for "redefine[ing] 'meaningfully close personal relationship' in subjective rather than objective terms," the dissent argued that *Dirks* required courts to "focus on objective criteria" when analyzing the personal benefit element: "The question for a finder of fact is not whether the insider . . . wished good on the tippee, but whether she received something in return for her tip."[19] Pooler concluded that the majority's opinion improperly "render[ed] *Newman* a relic" and abrogated a prior circuit decision through a panel opinion.[20] As a result, she opined, the majority opinion had limited precedential value: "Bare speculation into insiders' motives has always been insufficient; it remains so today in spite of the majority's dicta."[21] Pooler warned of unintentional consequences for the market, noting that "[t]he conservative thing [for traders, journalists and analysts] to do would be to avoid seeking inside information too aggressively, even if the whole market could benefit from such investigation."[22]

The full Circuit ultimately declined, in August 2018, to rehear Martoma's case. Until the full Second Circuit or the Supreme Court elaborates further on the "meaningfully close personal relationship" standard, insider trading defendants will grapple with the question raised by Judge Pooler: whether any practical limitations remain on the gift theory of personal benefit or whether the rule has become "a mere formality."[23]

SEC Enforcement Co-Director Emphasizes Nonmonetary Relief in SEC Actions

On October 3, 2018, Steven Peikin, the Co-Director of the Division of Enforcement (the "Division") of the U.S. Securities and Exchange Commission, provided his view on the recently concluded SEC fiscal year and priorities for the Division in terms of remedies and relief sought.

Pushing back against metrics that measure the Division's effectiveness based on the number of cases brought and penalty dollars imposed (and thereby suggesting a continuation of the downward trend in both numbers), Director Peikin highlighted nonmonetary remedies that the Division has used to pursue its priorities of (1) protecting retail investors; (2) holding individuals accountable; and (3) furthering Division goals of punishing wrongdoing and preventing future investor harm. In particular, Director Peikin discussed the ability of the Commission to seek undertakings and conduct-based injunctions as well as bars and suspensions for individuals (from, for example, serving as an officer or director of a public company). As an example, he highlighted the nonmonetary sanctions recently imposed against Tesla and its Chairman and CEO Elon Musk, including the requirement that Musk resign as chairman, the addition of two independent directors to the Tesla Board of Directors and enhanced compliance procedures around public statements.

Director Peikin stressed, however, the continued importance of penalties as an enforcement tool, especially against SEC-regulated entities. For corporate issuers, by contrast, he expressed caution, saying the imposition of penalties "require[s] careful and thoughtful balancing." Indeed, he highlighted examples of the Division not imposing penalties where management identified, self-reported and self-remediated potential wrongdoing. Director Peikin noted that "disgorgement is handled quite differently. Even when a defendant or respondent cooperates and agrees to meaningful undertakings, it should not be entitled to keep its ill-gotten gains."

Director Peikin's remarks should offer some comfort to public company issuers that current SEC leadership is not aggressively seeking large penalties against issuers for securities law violations. At the same time, his remarks should further incentivize issuers to put in place robust controls, policies and procedures to ensure compliance with securities laws and regulations, including procedures to protect material nonpublic information and guard against trading on the same.

Update on *Morrison*: Building Section 10(b)'s Border Wall

Earlier this year, the Ninth Circuit issued its opinion in *Stoyas v. Toshiba Corporation*,[1] the latest installment of federal appellate court decisions interpreting the Supreme Court's *Morrison* transactional test. While *Toshiba* focused on a technical application of *Morrison* to American Depositary Receipts ("ADRs"), the Ninth Circuit's opinion illustrated the continued evolution of the territorial gates *Morrison* erected around Section 10(b) of the Exchange Act.

The Supreme Court's *Morrison* decision involved a securities claim brought by foreign investors who purchased shares of a foreign bank on a foreign exchange—sometimes referred to as a "foreign cubed" claim.[2] The *Morrison* Court held that Section 10(b) lacks extraterritorial reach, and dismissed the claims in question.[3] In doing so, the *Morrison* Court propounded a new two-pronged standard by which to determine the applicability of Section 10(b): Does the transaction involve (1) "the purchase or sale of a security listed on an American stock exchange" or (2) "the purchase or sale of any other security in the United States."[4] Since *Morrison*, the lower federal courts have been tasked with defining the contours of Section 10(b)'s border wall.

Purchases and Sales "In the United States"

The "irrevocable liability" test, established by the Second Circuit in *Absolute Activist*,[5] is widely accepted as the standard to determine whether a transaction involves "the purchase or sale of any other security in the United States."[6] The test focuses on where irrevocable liability to take and pay for, or deliver, a security is incurred.[7] This can be, for example, the place where title is transferred, a contract is formed, a purchase order is placed or money is exchanged.[8] Subsequent decisions have further refined the application of "irrevocable liability" to the realities of modern, global securities markets. In most instances, the lower courts have added more bricks to the wall.

For instance, in *City of Pontiac Policemen's and Firemen's Retirement System v. UBS AG*, the Second Circuit held that Section 10(b) does not apply to a "foreign squared" claim in which a U.S.-based investor purchased securities of a foreign company on a foreign exchange, concluding that a purchaser's physical location when a purchase order is placed is not equivalent to the location of a securities transaction.[9] Courts have also consistently held that domestic "actions needed to carry out transactions"—including transfers

Continued on page 14

Update on *Morrison*: Building Section 10(b)'s Border Wall
Continued from page 13

of beneficial ownership via domestic securities depositories, such as the Depositary Trust Company—are not, standing alone, within the ambit of Section 10(b).[10] The securities class action bar was also put on notice by the Second Circuit in *In re Petrobras Securities*. In vacating the district court's certification of the class, the Second Circuit questioned whether members of a putative class could satisfy Rule 23(b)(3)'s predominance requirement given the "plaintiff-specific nature of the *Morrison* inquiry."[11] And, in a case with potential implications for cross-border mergers and acquisitions, the Second Circuit held that the location of U.S.-based shareholders who receive securities pursuant to a merger of foreign companies is not relevant to determining the locus of the securities transaction, as the shareholders are not parties to the actual merger transaction.[12]

Purchases and Sales "on an American Stock Exchange"

Although less has been written about the "purchase or sale of a security listed on an American stock exchange" prong of *Morrison*, the Second Circuit delivered a significant victory to dual-listed issuers in *City of Pontiac*. Reasoning that the *Morrison* Court focused on the location of the securities transaction, not the location of any exchange on which an issuer's securities are listed, the Second Circuit held that a U.S. listing will not serve as a domestic anchor for purposes of Section 10(b) if the transactions at issue were executed on a foreign exchange.[13]

Of somewhat more academic interest, the application of *Morrison* to interdealer quotation systems such as the "OTC Markets" or "Pink Sheets" has resulted in a potential conflict between the Third and Ninth Circuits. Whereas the text of Section 10(b) includes the words "national securities exchange," the *Morrison* Court held that Section 10(b) reaches "domestic" or "American" exchanges.[14] The Third Circuit easily concluded that the OTC Bulletin Board and Pink Sheets do not meet *Morrison*'s definition of "American stock exchange" by relying on the SEC's public list of registered national securities exchanges.[15] On the other hand, the Ninth Circuit questioned whether the *Morrison* Court's text was truly "shorthand" for "national securities exchanges," or if the Court intentionally distinguished "American" exchanges due to the territorial nature of the *Morrison* transaction-based test.[16] Nonetheless, the Ninth Circuit concluded that "OTC Link" is not an "exchange" as defined in the Exchange Act and therefore held that transactions in securities listed on OTC Link, such as the ADRs in question, were not transactions "on an American Stock Exchange."[17]

Lucia v. SEC: Supreme Court Rejects Constitutionality of SEC ALJs

On June 21, 2018, the U.S. Supreme Court held in *Raymond James Lucia Cos. Inc. et al. v. U.S. Securities and Exchange Commission* that administrative law judges ("ALJs") of the United States Securities and Exchange Commission are "inferior Officers" of the United States and therefore must be appointed by the Commission itself, rather than the Commission's staff.[1] The decision reversed a prior ruling by the U.S. Court of Appeals for the District of Columbia Circuit, which had held that ALJs are "mere employees" and therefore do not constitute inferior Officers within the meaning of the Appointments Clause.[2]

The *Lucia* Opinion

The Supreme Court opinion, authored by Justice Elena Kagan, explained that the Court's prior precedent on the special trial judges of the United States Tax Court compelled the conclusion that SEC ALJs similarly constitute inferior Officers.[3] The opinion cites the ALJs' "extensive powers" over discovery, subpoenas, motions, admission of evidence, administration of oaths, witness examinations, and sanctions in concluding that ALJs, like federal trial judges, exercise sufficient authority to fall within the constitutional category of inferior Officer.[4] The finality of the ALJs' decisions along with their career appointments and "significant discretion" further supported the Court's analysis. Because the ALJs were not properly appointed at the time of Lucia's proceeding, the Court remanded the case for a new proceeding and ordered that Lucia's original ALJ not oversee the new proceeding "even if he has by now received (or receives sometime in the future) a constitutional appointment."[5]

The majority opinion in *Lucia* appears to cast doubt on the sufficiency of a November 2017 Commission order that retroactively "ratified" the appointments of five ALJs.[6] In a footnote, the majority opinion stated that although Lucia challenged the validity of the ratification, the Court saw no reason to address that issue because the Commission "has not suggested that it intends to assign Lucia's case to an ALJ whose claim to authority rests on the ratification order."[7] The Court further stated that the SEC could decide to conduct the rehearing itself, or assign the rehearing to an ALJ "who has received a constitutional appointment independent of the ratification,"[8] which suggests that the majority does not believe the ratification was sufficient.

Lucia's Aftermath

Immediately following the ruling, the Commission issued an order staying all administrative proceedings for the next 30 days to provide it with additional time to consider reappointing the ALJs. However, on August 22, 2018, the Commission issued another order (the

Continued on page 16

***Lucia v. SEC*: Supreme Court Rejects Constitutionality of SEC ALJs**

Continued from page 15

"August 2018 Order") lifting its stay on pending administrative proceedings and reaffirming the November 2017 ratification.[9] Whether the ratification will be ultimately found to be valid is unclear. As a result of the August 2018 Order, respondents in nearly 200 SEC proceedings with pending cases were given the opportunity for a new hearing before an ALJ who did not previously participate in the matter.

Moreover, the Supreme Court's emphasis on Lucia's "timely challenge" implies that respondents who have not brought timely challenges, including individuals who have settled with the SEC, may be left empty-handed by the ruling. The Court, however, has also occasionally exercised its discretion—including in a decision that the Court relied on in *Lucia*—to consider claims that were not timely raised but that nonetheless implicate "the strong interest of the federal judiciary in maintaining the constitutional plan of separation of powers."[10] Therefore, it is possible that respondents who did not timely raise the issue could seek relief in federal courts now that the Supreme Court has decided the issue as a matter of constitutional—rather than statutory—rights. Otherwise, however, the door could be closed to respondents who settled or did not timely challenge the authority of the relevant ALJs.

The constitutionality of the statutory restrictions on removal of ALJs also remains open to challenge. The SEC's ALJs are removable only for cause by the SEC Commissioners, who themselves are removable only for cause. The Solicitor General filed a brief in *Lucia* urging the Court to follow the 2010 decision in *Free Enterprise Fund v. Public Company Accounting Oversight Board*,[11] which held that the dual layer of removal protections afforded to PCAOB members was unconstitutional because it interfered with the President's executive power.[12] However, the Court expressly declined to address this issue in *Lucia*, noting that it "ordinarily await[s] thorough lower court opinions to guide [its] analysis of the merits."[13] Interestingly, when *Free Enterprise Fund* was first heard by the D.C. Circuit, Justice Kavanaugh authored a dissenting opinion that was ultimately adopted by the Court.

Unanswered Questions

Lucia leaves several other questions unanswered, including the decision's impact on ALJs across the administrative bureaucracy. Although six of the Justices joined in the decision, their reasoning differed, with less than half of the Court joining in Justice Kagan's opinion. Justice Breyer concurred in part with the judgment, but argued that the case should have been decided based on the Administrative Procedure Act, so as to avoid the constitutional question. Justice Thomas, joined by Justice Gorsuch, also concurred in the judgment, but provided an alternative rationale based on an originalist reading of the Appointments

Continued on page 17

***Lucia v. SEC*: Supreme Court Rejects Constitutionality of SEC ALJs**

Continued from page 16

Clause. Because the basis for the decision varies by Justice, the analysis may play out differently when applied to other agencies' administrative judges who exhibit different characteristics and exercise different levels of authority. Moreover, given that Supreme Court Justices Gorsuch and Kavanaugh are skeptical of the *Chevron* doctrine, *Lucia*'s implications remain in flux.

The SEC may continue to decrease its use of administrative proceedings—as it has already done over the past couple of years—and instead choose to litigate significant contested matters in federal court, so as to avoid additional high-stakes appeals of its ALJ decisions. Of course, certain causes of action are only available in administrative proceedings, such as failure to supervise and violations of Rule 102(e) of the SEC Rules of Practice, so these types of proceedings will continue to be litigated as administrative proceedings. The federal courts may look even more inviting to the SEC because the *Lucia* decision follows a handful of losses by the SEC in administrative proceedings, which have raised questions about whether administrative proceedings are as advantageous to the SEC as previously believed.

SEC Adopts Amendments to Simplify and Update Disclosure Requirements

On August 17, 2018, the Securities and Exchange Commission adopted final rules to amend or eliminate certain disclosure requirements that have become redundant, duplicative, overlapping, outdated or superseded in light of other SEC disclosure requirements, U.S. Generally Accepted Accounting Principles ("GAAP") or changes in the information environment. The amendments are effective for all filings made on or after November 5, 2018.

The amendments are part of the SEC's ongoing efforts to review its disclosure requirements to simplify the disclosure regime without significantly changing the total mix of information provided to investors. The amendments eliminate certain requirements that mandate disclosures that are redundant or duplicative of other SEC, U.S. GAAP or International Financial Reporting Standards disclosure requirements. For instance, the SEC eliminated the requirements in Regulation S-X to identify related-party transactions because the same disclosures are required under Regulation S-K and U.S. GAAP. The amendments also modified or eliminated disclosure requirements which overlap with, but

Continued on page 18

SEC Adopts Amendments to Simplify and Update Disclosure Requirements

Continued from page 17

are not identical to, other disclosure requirements in cases where reasonably similar disclosure would be elicited as a result of compliance with other such disclosure requirements. To the extent that such requirements overlapped with U.S. GAAP, the SEC ultimately referred the overlapping SEC disclosure requirements that require incremental information to the Financial Accounting Standards Board ("FASB") for FASB to determine whether to include these items on its agenda for potential incorporation into U.S. GAAP. Finally, the SEC amended or eliminated requirements which are outdated as a result of the availability of information due to technological advances and conformed other disclosure requirements to more recently updated SEC or U.S. GAAP requirements.

As a result of the amendments, certain disclosures may be relocated within a filing. Disclosure which was previously located outside of the financial statements and is relocated within the financial statements may become subject to annual audit or interim review as well as internal controls over financial reporting, and the safe harbor for forward-looking statements under the Private Securities Litigation Reform Act of 1995 will no longer be available. For information that was previously located within the financial statements and is moved outside of the financial statements, the opposite effect applies.

The SEC also published a Compliance and Disclosure Interpretation related to Exchange Act Forms (C&DI Question 105.09) to provide guidance regarding the new requirement to present changes in stockholders' equity and dividends per share for each class of shares for interim periods. C&DI Question 105.09, as updated, states that the SEC would not object if a filer first presented the changes in stockholders' equity in its Form 10-Q for the quarter beginning after November 5, 2018. Therefore, a December 31 fiscal year-end filer may omit the disclosure from its Form 10-Q for the quarter ended September 30, 2018, and a June 30 fiscal year-end filer may omit the disclosure from its Forms 10-Q for the quarters ended September 30, 2018 and December 31, 2018.

These simplification and updating efforts are intended to help investors make more efficient investment decisions and reduce issuer compliance costs, ultimately promoting capital formation. The SEC will report on the impact of these amendments no later than five years after the effective date.

For a high-level summary of certain notable amendments adopted by the SEC, see the chart beginning on the following page.

Continued on page 19

Certain Notable Amendments from the Final SEC Rules*

Topic	Rule	Pre-Release Requirement	Amendment
Derivative Accounting Policies	Rule 4-08(n) and Note 2(b) to Rule 8-01 of Regulation S-X	Required disclosure related to derivative instruments of, where material, the applicable accounting policies and the criteria applicable to such policies, as well as how the derivative instruments are reported in the financial statements	Eliminates most of the requirements of Rule 4-08(n) except the requirement to disclose where in the statement of cash flows the effect of derivative financial instruments is reported
Research and Development Activities	Items 101(c)(1)(xi) and 101(h)(4)(x) of Regulation S-K; Item 5.C of Form 20-F; Item 7(a)(1)(iii) of Form 1-A	Required the disclosure, if material, of the amount spent on research and development for all years presented	Eliminates disclosure requirement of Items 101(c)(1)(xi) and 101(h)(4)(x) of Regulation S-K; Item 5.C of Form 20-F; Item 7(a)(1)(iii) of Form 1-A
Ratio of Earnings to Fixed Charges	Items 503(d) and 601(b)(12) of Regulation S-K; Instruction 7 of Form 20-F	Required issuers that register debt securities to disclose the historical and pro forma ratios of earnings to fixed charges; required issuers that register preference equity securities to disclose the historical and pro forma ratio of combined fixed charges and preference dividends to earnings; required filing of an exhibit setting forth the computation of the above ratio	Eliminates the requirement to disclose ratio of earnings to fixed charges and the corresponding exhibit in Items 503(d) and 601(b)(12) of Regulation S-K and Instruction 7 of Form 20-F
Interim Financial Statements – Pro Forma Business Combination Information	Rules 8-03(b)(4) and 10-01(b)(4) of Regulation S-X	Required disclosure in the notes to interim financial statements of pro forma information for "significant" business combinations for smaller reporting companies and Regulation A issuers in a Tier 2 offering and for "material" business combinations for other companies; required line item disclosure of pro forma revenue, net income, net income attributable to the issuer and net income per share	Eliminates the requirement to include pro forma financial information in interim filings for business combinations in Rules 8-03(b)(4) and 10-01(b)(4) as proposed

* This chart is intended to provide an overview of certain key amendments adopted by the SEC, and is not intended to be a comprehensive chart of all amendments.

Continued on page 20

Certain Notable Amendments from the Final SEC Rules*

Topic	Rule	Pre-Release Requirement	Amendment
Segments	Item 101(b) of Regulation S-K and Item 7(b) of Form 1-A	Required disclosure of segment financial information, restatement of prior periods when reportable segments change and discussion of interim segment performance that may not be indicative of current or future operations	Eliminates Item 101(b) of Regulation S-K and Item 7(b) of Form 1-A
Geographic Areas	Items 101(d)(1), 101(d)(2) and 101(d)(3) of Regulation S-K	Required disclosure of financial information by geographic area and disclosure of any risks associated with an issuer's foreign operations and any segment's dependence on foreign operations	Eliminates the requirements in Item 101(d)(1)-(3) and amends Item 303(a) of Regulation S-K to add an explicit reference to "geographic areas"
Seasonality	Instruction 5 to Item 303(b) of Regulation S-K	Required a discussion of any seasonal aspects of an issuer's business where the effect is material	Eliminates Instruction 5 to Item 303(b) of Regulation S-K
Market Price Disclosure	Item 201(a)(1) of Regulation S-K; Item 9.A.4 of Form 20-F	Required disclosure of the principal U.S. market where equity is traded, required foreign issuers to disclose the principal established foreign public trading market (if applicable) and required the high and low sale prices or bid prices for each quarter within the two most recent fiscal years and subsequent interim period	Eliminates the requirement to disclose sale or bid prices for most issuers whose common equity is traded in an established public trading market and replace it with the disclosure of the trading symbol. Form 20-F is amended to be consistent with the amendments to Item 201(a)(1) of Regulation S-K.
Available Information – Public Reference Room	Item 101(e)(2) and Item 101(h)(5)(iii) of Regulation S-K; Forms S-1, S-3, S-4, S-11, F-1, F-3 and F-4; Item 1118(b) of Regulation AB; and Forms SF-1 SF-3 N-1A, N-2, N-3, N-5, N-6 and N-8B-2	Applicable provisions required issuer to identify the Public Reference Room and disclose its physical address and phone number	Eliminates the requirements to identify the Public Reference Room and disclose its physical address and phone number. Also eliminates the instruction in certain N-Forms on how to send a written request by mail to the SEC's Public Reference Room to obtain certain hard copy information.
Available Information – Issuer Internet Address	Item 101(e) and Item 101(h)(5) of Regulation S-K; and Forms S-3, S-4, F-1, F-3, F-4, 20-F, SF-1 and SF-3	Required accelerated and large accelerated filers to disclose their Internet address, if they have one	Expands requirement to apply to all issuers

* This chart is intended to provide an overview of certain key amendments adopted by the SEC, and is not intended to be a comprehensive chart of all amendments.

Notes

Cyan, Inc. v. Beaver Cty. Employees Ret. Fund: Supreme Court's Decision Raises Spectre of More Item 303 Disclosure Claims in State Court

1. *Cyan Inc. v. Beaver County Employees Retirement Fund*, 138 S. Ct. 1061 (2018).
2. *Id.* at 1066.
3. *Id.*
4. *Id.* at 1066–67.
5. *Id.*
6. *Id.*; *see also* 15 U.S.C. § 77p(c).
7. *Id.* at 1068.
8. *Id.*
9. *Id.*
10. *Id.* at 1068-69.
11. *Id.* at 1078.
12. *Id.* at 1069.
13. 15 U.S.C. § 78aa.
14. *Id.* at 1072.
15. *Id.* at 1069.
16. *Id.* at 1075.
17. The Court explained that Section 77p(c) allows for removal of "[a]ny covered class action brought in any State court involving a covered security, as set forth in subsection (b)." The covered class actions "set forth" in § 77p(b) are state-law class actions alleging securities misconduct. Because federal lawsuits are not "class action[s] . . . as set forth in subsection (b)," they remain subject to the 1933 Act's removal ban.
18. *Id.* at 1078.
19. 15 U.S.C. §§ 77k, 77l(a)(2).
20. *Panther Partners Inc. v. Ikanos Commc'ns, Inc.*, 681 F.3d 114, 119 (2d Cir. 2012).
21. *Indiana Pub. Ret. Sys. v. SAIC, Inc.*, 818 F.3d 85, 94 (2d Cir. 2016), *cert. granted sub nom. Leidos, Inc. v. Indiana Pub. Ret. Sys.*, 137 S. Ct. 1395, 197 L. Ed. 2d 553 (2017), and *cert. dismissed sub nom. Leidos, Inc. v. Indiana Pub. Ret. Sys.*, 138 S. Ct. 2670 (2018) (citing 17 C.F.R. § 229.202(a)(3)(ii)).
22. *Id.* (quoting *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 101 (2d Cir. 2015)).
23. *Id.* at 95.
24. *Id.* at 96 (emphasis added).
25. *In re Barclays Bank PLC Sec. Litig.*, No. 09 Civ. 1989, 2017 WL 4082305, at *13 (S.D.N.Y. Sept. 13, 2017).
26. *Id.* at *13-14.
27. *Id.* at *14.
28. *Litwin v. Blackstone Grp., L.P.*, 634 F.3d 706, 720 (2d Cir. 2011).
29. *Id.* at 716.
30. *Panther Partners Inc. v. Ikanos Commc'ns, Inc.*, 681 F.3d 114, 117 (2d Cir. 2012).
31. *Id.* at 22.
32. *Leidos, Inc. v. Indiana Pub. Ret. Sys.*, 137 S. Ct. 1395 (2017).
33. *Leidos, Inc. v. Indiana Pub. Ret. Sys.*, 138 S. Ct. 2670 (2018).
34. *See Indiana Pub. Ret. Sys. v. SAIC, Inc.*, 818 F.3d 85, 88 (2d Cir. 2016), *cert. granted sub nom. Leidos, Inc. v. Indiana Pub. Ret. Sys.*, 137 S. Ct. 1395 (2017), and *cert. dismissed sub nom. Leidos, Inc. v. Indiana Pub. Ret. Sys.*, 138 S. Ct. 2670 (2018); *Stratte-McClure v. Morgan Stanley*, 776 F.3d 94, 101 (2d Cir. 2015).
35. *See In re NVIDIA Corp. Sec. Litig.*, 768 F.3d 1046, 1048 (9th Cir. 2014); *Oran v. Stafford*, 226 F.3d 275 (3d Cir. 2000).

Continued on page 22

SEC Spotlight on Cybersecurity

1. https://www.sec.gov/litigation/investreport/34-84429.pdf.
2. *See* https://www.sec.gov/news/public-statement/statement-clayton-2018-02-21; https://www.sec.gov/news/press-release/2018-22.
3. https://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm.
4. https://www.sec.gov/rules/interp/2018/33-10459.pdf.
5. *Id.*
6. https://www.sec.gov/news/press-release/2018-71.
7. *Id.*
8. *Id.*
9. https://www.sec.gov/news/press-release/2018-213.
10. https://www.sec.gov/litigation/admin/2018/34-84288.pdf.
11. https://www.sec.gov/news/speech/speech-stein-092718.
12. *Id.*
13. *See* https://www.marketwatch.com/story/sec-brings-second-insider-trading-case-over-equifax-data-breach-2018-06-28; https://www.nytimes.com/2018/06/28/business/equifax-insider-trading-sec.html.
14. *See* Public Statement on Cybersecurity: https://www.sec.gov/news/public-statement/statement-clayton-2017-09-20.

United States v. Martoma: Second Circuit Declines Rehearing in Case Analyzing *Salman's* Scope

1. 137 S. Ct. 420 (2016).
2. 773 F.3d 438 (2d Cir. 2014).
3. No. 14-3599 (2d Cir. 2017).
4. 773 F.3d 438 (2d Cir. 2014).
5. In *Dirks*, the Supreme Court established that an insider tipper may receive a personal benefit where she "makes a gift of confidential information to a trading relative or friend," on the reasoning that such a gift was akin to trading by the tipper followed by a gift of the proceeds. 463 U.S. 646, 664 (1983).
6. *Newman*, 773 F.3d at 452.
7. 137 S. Ct. at 422.
8. *U.S. v. Martoma*, 869 F.3d 58, 69 (2d Cir. 2017) (citing *Salman*, 137 S. Ct. at 428) (internal quotation marks omitted).
9. *Id.* at 72 (citing *Salman*, 137 S. Ct. at 427-28 and *Dirks*, 463 U.S. at 664).
10. *Id.* at 61.
11. *Id.* at 75, 92 (Pooler, J., dissenting).
12. *Id.* at 85–86.
13. *Id.* at 87.
14. *U.S. v Martoma*, 894 F.3d 64, 77 (2d Cir. 2017) (as amended June 25, 2018).
15. *Id.* at 75–76.
16. *Id.* at 76.
17. *Id.* at 71.
18. *Id.* at 80 (Pooler, J., dissenting).
19. *Id.* at 80, 81 (Pooler, J., dissenting).
20. *Id.* at 80 (Pooler, J., dissenting).
21. *Id.* at 81 (Pooler, J., dissenting).
22. *Id.* at 81–82 (Pooler, J., dissenting).
23. *Id.* at 81 (Pooler, J., dissenting).

Continued on page 23

Update on *Morrison*: Building Section 10(b)'s Border Wall

1. 896 F.3d 933 (9th Cir. 2018). On October 15, 2018 Toshiba filed a petition for *writ of certiorari* seeking Supreme Court review of the Ninth Circuit's decision.
2. *Morrison v. National Australia Bank, Ltd.* 130 S. Ct. 2869 (2010).
3. *Id.*
4. *Id.*
5. *Absolute Activist Value Master Fund Ltd. v. Ficeto*, 677 F.3d 60 (2d Cir. 2012).
6. The "irrevocable liability" test has been expressly adopted by the Third and Ninth Circuits in *U.S. v. Georgiou*, 777 F.3d 125 (3d Cir. 2015) and *Stoyas v. Toshiba Corp.*, 896 F.3d 933 (9th Cir. 2018), respectively.
7. *Absolute Activist*, 677 F.3d at 68.
8. *Id.* at 70.
9. *City of Pontiac Policemen's and Firemen's Retirement System v. UBS AG*, 752 F.3d 173 (2d Cir 2014).
10. *Loginavskaya v. Batratchenko*, 764 F.3d 266, 275 (2d Cir. 2014); *In re Petrobras Sec. Litig.*, 150 F. Supp. 3d 337, 342 (S.D.N.Y. 2015).
11. *In re Petrobras Securities*, 862 F.3d 250, 271–75 (2d Cir. 2017).
12. *In re Vivendi, S.A. Sec. Litig.*, 838 F.3d 223, 265 (2d Cir. 2016).
13. *City of Pontiac*, 752 F.3d at 180.
14. *Morrison*, 130 S. Ct. 2869.
15. *Georgiou*, 777 F.3d at 134–35.
16. *Toshiba Corp.*, 896 F.3d 933 at 945–47.
17. *Id.* at 947. However, transactions executed on interdealer quotation systems may constitute a "purchase or sale of any other security in the United States" under the second prong of *Morrison*. For instance, the Third Circuit has concluded that a foreign buyer or seller incurs "irrevocable liability" within the United States by executing trades via a U.S.-based market maker in OTC-listed securities. *Georgiou*, 777 F.3d at 136–37.

Lucia v. SEC: Supreme Court Rejects Constitutionality of SEC ALJs

1. *Lucia et al. v. Sec. Exch. Comm'n*, No. 17-130, 585 U.S. __ (2018).
2. *Raymond J. Lucia Cos., Inc. v. Sec. Exch. Comm'n*, 832 F.3d 277 (D.C. Cir. 2016).
3. *See Freytag v. Comm'r,* 501 U.S. 868 (1991).
4. *Lucia et al. v. Sec. Exch. Comm'n*, No. 17-130, 585 U.S. __ at *2 (2018).
5. *Id.* at *12.
6. *See* Press Release, Sec. Exch. Comm'n, SEC Ratifies Appointment of Administrative Law Judges (Nov. 30, 2017), available at https://www.sec.gov/news/press-release/2017-215.
7. *Lucia et al. v. Sec. Exch. Comm'n*, No. 17-130, 585 U.S. __ at *13, fn. 6 (2018).
8. *Id.*
9. *Order, In re : Pending Administrative Proceedings*, Release No. 10510 (June 21, 2018).
10. *See, e.g., Freytag v. Comm'r*, 501 U.S. 868, 879 (1991).
11. *Free Enterprise Fund*, 561 U.S. 477 (2010).
12. Brief for Respondent Supporting Petitioners at 44–45, *Lucia et al. v. Sec. Exch. Comm'n*, 585 U.S. __ (2018) (No. 17-130).
13. *Lucia et al. v. Sec. Exch. Comm'n*, No. 17-130, 585 U.S. __ at 4 n. 1 (2018) (internal citations and quotation marks omitted).

Insider Trading & Disclosure Update

Insider Trading & Disclosure Update is a publication of Debevoise & Plimpton LLP

New York
919 Third Avenue
New York, New York 10022
+1 212 909 6000
www.debevoise.com

Washington, D.C.
801 Pennsylvania Avenue N.W.
Washington, D.C. 20004
+1 202 383 8000

London
+44 20 7786 9000

Paris
+33 1 40 73 12 12

Frankfurt
+49 69 2097 5000

Moscow
+7 495 956 3858

Hong Kong
+852 2160 9800

Shanghai
+86 21 5047 1800

Tokyo
+81 3 4570 6680