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## Wall Street as Yossarian: The Other Effects of the Rajaratnam Insider Trading Conviction

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## WALL STREET AS YOSSARIAN: THE OTHER EFFECTS OF THE RAJARATNAM INSIDER TRADING CONVICTION

*J. Scott Colesanti\**

### I. INTRODUCTION

*“Without warning, the patient sat up in bed and shouted, ‘I see everything twice!’”<sup>1</sup>*

And thus Yossarian, the war-weary bomber pilot of the masterful novel, *Catch-22*, was able to malingering in an Italian hospital even longer while nervous doctors attended to the strange malady of his neighbor.<sup>2</sup>

The storied literary diversion may highlight the good fortune of those evading government prosecution of financial crimes in 2011, a year that fulfilled the promise that observers of hedge fund discipline would similarly see things twice. To wit, in May 2011, a Manhattan jury convicted billionaire hedge fund entrepreneur Raj Rajaratnam of fourteen counts of conspiracy and securities fraud.<sup>3</sup> Chief among these convictions was the crime of insider trading.<sup>4</sup> The case punctuated two years of criminal actions based upon insider trading allegations by the U.S. Attorney for the Southern District of New York, who had called

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1. JOSEPH HELLER, *CATCH-22*, at 177 (1989).

2. *See id.* at 176-78.

3. Peter J. Henning, *How Serious a Crime Is Insider Trading?*, DEALBOOK (Aug. 10, 2011, 3:30 PM), <http://dealbook.nytimes.com/2011/08/10/how-serious-a-crime-is-insider-trading/>; Peter Lattman, *Galleon Chief Sentenced to 11-Year Term in Insider Case*, DEALBOOK (Oct. 13, 2011, 9:14 PM), <http://dealbook.nytimes.com/2011/10/13/rajaratnam-is-sentenced-to-11-years/>.

4. Lattman, *supra* note 3.

Rajaratnam “the modern face of illegal insider trading.”<sup>5</sup> Perhaps more significantly, five months later, Judge Richard J. Holwell sentenced Rajaratnam to eleven years in prison,<sup>6</sup> in handing down the harshest sentence ever in such a case.<sup>7</sup>

The Rajaratnam trial was the climax to a prolonged investigation that resulted in the conviction of over two dozen hedge fund workers and public company/financial firm employees for their roles in a \$50 million scheme.<sup>8</sup> The case also emphasized the unforgiving nature of securities fraud accusations where those who should know better (for example, attorneys) were concerned, as lawyers ensnared in the net cast at the fallen Galleon Management, LP (“Galleon”) received consistently glaring prison sentences.<sup>9</sup> Further, the Rajaratnam conviction seemingly reverberated through the courts, leading to strict interpretations of procedural rules attending unrelated insider trading cases.<sup>10</sup>

But the celebrated conviction failed to end the parallel U.S. Securities and Exchange Commission (the “SEC” or the “Commission”) investigation, litigation, or its pursuit of both fine and disgorgement.<sup>11</sup> Thus, while commentators accurately noted that the use of Department

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5. *Ex-Hedge Fund Boss Sentenced to 11 Years in Prison*, NPR (Oct. 13, 2011), <http://www.npr.org/2011/10/13/141311454/u-s-seeks-record-sentence-for-ex-hedge-fund-boss> (internal quotation marks omitted); Lattman, *supra* note 3 (detailing charges against fifty-four individuals, fifty of whom either pleaded guilty or were convicted).

6. *Ex-Hedge Fund Boss Sentenced to 11 Years in Prison*, *supra* note 5; Lattman, *supra* note 3.

7. Lattman, *supra* note 3. While another defendant in the scheme focusing on Galleon Management, LP previously received a ten-year sentence, the article notes that “[t]he average sentence of the 13 other defendants connected to Mr. Rajaratnam’s case has been about three years.” *Id.*

8. *Judge Sentences Hedge Fund Worker to Prison*, N.Y. L.J., Sept. 1, 2011, at 1 (detailing the six and a half year sentence meted to hedge fund worker Craig Drimal for his role in “the largest hedge fund insider-trading case in history”). Speaking more globally, in 2010 and 2011, Manhattan prosecutors charged fifty-two individuals with insider trading, forty-nine of whom pleaded guilty or were convicted. Peter Lattman, *Latest Trial Set to Begin in Insider Trading Inquiry*, DEALBOOK (Aug. 30, 2011, 8:22 PM), <http://dealbook.nytimes.com/2011/08/30/latest-trial-set-to-begin-in-insider-trading-inquiry/>.

9. See, e.g., Mark Hamblett, *Another Attorney Sentenced in Insider Trading Scheme*, N.Y. L.J., Oct. 13, 2011, at 1 (describing the sentences of lawyer defendants of prison terms ranging from two and a half years to ten years for their roles in trading money for inside information stolen from the law firm of Ropes & Gray LLP). The judge noted that one of the lawyer attorneys (although non-practicing) “[u]nderstood better than most the illegality of this kind of conduct.” *Id.* (internal quotation marks omitted).

For purposes of this Article, the term “inside information” is interchangeable with its juridical counterpart, “material, non-public information.”

10. See, e.g., *United States v. Gansman*, 657 F.3d 85, 90-92, 94-95 (2d Cir. 2011) (finding no reversible error in insider trading case where, inter alia, the trial judge permitted cross examination on polygraph tests as well as a “slightly modified version of the charge” to the jury where the charge requested by the defense and decrying polygraph tests were equally permissible).

11. See discussion *infra* Part II.C.

of Justice (“DOJ”) wiretaps changed the nature of both the game and the results for Wall Street’s illegal players,<sup>12</sup> receiving less attention is the delaying effect the trial had—both on clarifying insider trading law and questioning the unchecked use of government resources.<sup>13</sup> While no one could quibble with the efficiency of the DOJ’s results, this Article seeks to reveal their equally significant effects on the government’s ongoing crusade against insider trading. Born via an administrative decision,<sup>14</sup> decades after the adoption of the securities laws themselves,<sup>15</sup> the uniquely American insider trading prohibition (and the attendant efforts of its chief enforcer) became perhaps a little more unique and problematic with the U.S. Attorney’s 2011 conviction of Rajaratnam.

## II. THE UNITED STATES (AND THE UNITED STATES) AGAINST RAJ RAJARATNAM

Rajaratnam was the founder and Managing General Partner of Galleon, a fourteen-year-old, multi-billion dollar adviser to a short list of eponymous hedge funds (“Galleon Funds”).<sup>16</sup> His success is well-chronicled in biblical terms; indeed, his net worth (and immigrant status) punctuate most stories of his downfall.<sup>17</sup>

### A. *The Accusations*

The SEC’s amended complaint (“2009 SEC Complaint”) filed in 2009 against Rajaratnam and Galleon named nineteen other entities and individuals (“Galleon Defendants”) alleged to form the hedge fund

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12. See, e.g., Ellen C. Brotman & Erin C. Dougherty, *Blue Collar Tactics in White Collar Cases*, CHAMPION, Sept. 2011, at 16, 16 (“Lawyers can expect white collar cases to be less about the paper and more about the snitches and their tape recordings.”).

13. See *id.* at 19-20 (quoting *Enforcement Cooperation Initiative*, SEC, <http://www.sec.gov/spotlight/enfcoopinitiative.shtml> (last modified Nov. 2, 2011)).

14. In *re* Cady, Roberts & Co., 40 S.E.C. 907, 907, 913-14 (1961) (affirming the SEC theory that trading on the basis of inside information constituted securities fraud).

15. See, e.g., ROBERTA S. KARMEL, REGULATION BY PROSECUTION: THE SECURITIES & EXCHANGE COMMISSION VS. CORPORATE AMERICA 55 (1982) (“The 1964 [federal securities law] amendments, . . . coupled with the legal principles enunciated in the *Cady, Roberts* case, changed the thrust and direction of securities law regulation and greatly expanded the SEC’s horizons.”). Professor Roberta Karmel, an SEC Commissioner between 1977 and 1980, has been an open and consistent critic of aggressive enforcement. *Id.* at 15-17, 259 (“[A]s I have repeatedly stressed, I do not believe that federal securities regulation is properly justifiable solely as a consumer protection device.”).

16. Amended Complaint and Demand for Jury Trial at 2, 8, SEC v. Galleon Mgmt., LP, 2011 WL 5374112 (S.D.N.Y. Nov. 8, 2011) (No. 09 Civ. 8811 (JSR)) [hereinafter 2009 SEC Complaint].

17. See George Packer, *A Dirty Business: New York City’s Top Prosecutor Takes on Wall Street Crime*, NEW YORKER, June 27, 2011, at 42, 42, 55 (“[The SEC] budget this year falls short of Raj Rajaratnam’s net worth at the time of his arrest.”).

chief's broad and ongoing network of corporate informants.<sup>18</sup> One Galleon Defendant was Danielle Chiesi, a registered broker and portfolio analyst at an investment adviser titled New Castle.<sup>19</sup> In sum, the SEC civil action concerned Rajaratnam's alleged activities in purchasing inside information regarding a dozen corporations from individuals placed within Intel Corporation, IBM, McKinsey & Company (a global consulting firm; "McKinsey"), and other companies.<sup>20</sup> Rajaratnam was said to have gleaned over \$33 million in profits from trading between 2006 and 2009 based upon the wrongfully obtained information.<sup>21</sup> The allegedly "tipped," nonpublic information concerned events ranging from corporate takeovers to imminent earnings reports, and the tips occasionally traveled through multiple parties.<sup>22</sup>

The two claims of the 2009 SEC Complaint sought relief based upon alleged violations of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act")<sup>23</sup> (and Rule 10b-5<sup>24</sup> promulgated thereunder) and Section 17(a) of the Securities Act of 1933 (the "Securities Act").<sup>25</sup> Rajaratnam and others were alleged to have violated all three subsections of Rule 10b-5; overall, Rajaratnam, was found to have acted illegally in three capacities—as a misappropriator (for having allegedly misappropriated material, nonpublic information via Galleon's representation on a board of directors), as a tippee (for utilizing improperly tipped information imparted by others for cash), and as a tipper (for, in turn, tipping illegally obtained information to the Galleon Funds).<sup>26</sup> On this last score, Rajaratnam and others were said to be "liable for the trading occurring in the funds advised—directly or indirectly—by each, respectively, because each effectuated the trades on

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18. 2009 SEC Complaint, *supra* note 16, at 2-6.

19. *Id.* at 2, 8.

20. *Id.* at 2.

21. See generally 2009 SEC Complaint, *supra* note 16.

22. *Id.* at 2. The following is a sample allegation: "A Polycom, Inc. ('Polycom') senior executive tipped Khan to material nonpublic information about Polycom's Fourth Quarter . . . 2005 and . . . 2006 earnings. Khan traded based on that information and, in turn, tipped Rajaratnam, who traded on behalf of Galleon based on that information." *Id.* at 3.

23. Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (2006).

24. 17 C.F.R. § 240.10b-5 (2011). Rule 10b-5's three subsections address, in turn, fraudulent schemes, misstatements, and practices. *Id.* The nearly seventy-year-old rule is the mechanism by which varied and novel forms of fraud are punished by regulators. LARRY D. SODERQUIST & THERESA A. GABALDON, SECURITIES REGULATION 424 (7th ed. 2010) ("The Commission adopted Rule 10b-5 in 1942 to close a gap in the anti-fraud provisions of the securities laws.").

25. Securities Act of 1933 § 17(a), 15 U.S.C. § 77q(a) (2006 & Supp. IV 2011). For many years, securities fraud has been charged by the Commission simultaneously under both Section 10(b) of the Exchange Act and Section 17(a) of the Securities Act. See *In re Lebed*, Securities Act Release Nos. 33-7891, 34-43307, 73 SEC Docket 741, 742 (Sept. 20, 2000).

26. 2009 SEC Complaint, *supra* note 16, at 45-48.

behalf of the funds, controlled the funds and/or unlawfully tipped the inside information to the funds.”<sup>27</sup>

Separately, the U.S. Attorney’s 2009 indictment of Rajaratnam (the “Indictment”)—unsealed the same day as the SEC announced its civil charges<sup>28</sup>—joined just one other defendant, Chiesi.<sup>29</sup> The Indictment detailed seven conspiracies between 2003 and 2009 involving Rajaratnam and others (some unnamed) to obtain inside information for purposes of profitable trading in public company stocks.<sup>30</sup> The Indictment named ten stocks traded between 2006 and 2009, and sought forfeiture by Chiesi and Rajaratnam of profits in excess of \$20 million.<sup>31</sup> In addition to alleging violations of all three subsections of Rule 10b-5,

27. *Id.* at 47. On October 26, 2011, the SEC filed a new civil complaint (“October 2011 Complaint”) naming Rajaratnam and Rajat Gupta, a former Director at McKinsey and a former Board member of The Procter & Gamble Company (“P & G”) and The Goldman Sachs Group (“Goldman Sachs”), as defendants. Complaint at 1, 20, SEC v. Gupta, No. 11 CIV 7566 (S.D.N.Y. Oct. 26, 2011). The October 2011 Complaint alleges that, in September 2008, Gupta tipped Rajaratnam material, nonpublic information concerning Goldman Sachs and P & G. *Id.* at 2. The Galleon Funds allegedly traded on the basis of this information consequently generated over \$23 million in profits. *Id.* Previously, Gupta defeated an attempt by the SEC to file an Order Instituting Public Administrative and Cease-and-Desist Proceedings (that is, an administrative complaint) against him, arguing that, by singling him out among the Galleon Defendants for internal SEC proceedings, the Commission had violated his rights under the Equal Protection Clause of the U.S. Constitution. Gupta v. SEC, 796 F. Supp. 2d 503, 506-07 (S.D.N.Y. 2011). Judge Jed S. Rakoff’s ruling against the SEC was again scathing: “A funny thing happened on the way to this forum. On March 1, 2011, the Securities and Exchange Commission . . .—having previously filed all of its Galleon-related insider trading actions in this federal district—decided it preferred its home turf.” *Id.* at 506.

28. Martin Flumenbaum & Brad S. Karp, *Disclosure of Wiretapped Conversations*, N.Y. L.J., Dec. 8, 2010, at 3.

29. Indictment, United States v. Rajaratnam, No. 09 Cr. 1184 (RJH) (S.D.N.Y. Dec. 15, 2009). Chiesi later pleaded guilty to three counts of securities fraud and received a sentence of thirty months. Susan Pulliam & Chad Bray, *Key Plotter Pleads Guilty in Galleon*, WALL ST. J., Jan. 20, 2011, at A1; Scott Schiffel, *Raj Rajaratnam Galleon Probe: Danielle Chiesi Sentenced for Insider Trading*, DAILY NEWS (July 20, 2011), [http://articles.nydailynews.com/2011-07-20/news/29814451\\_1\\_danielle-chiesi-mark-kurland-raj-rajaratnam-galleon](http://articles.nydailynews.com/2011-07-20/news/29814451_1_danielle-chiesi-mark-kurland-raj-rajaratnam-galleon). Several other of the Galleon Defendants lost their criminal trials in 2011. See Grant McCool, *Rajaratnam Wins Ruling, Wiretap Turnover on Hold*, REAL CLEAR MARKETS (Jan. 20, 2011), [http://www.realclearmarkets.com/news/reuters/finance\\_business/2011/Jan/20/rajaratnam\\_wins\\_ruling\\_wiretap\\_turnover\\_on\\_hold.html](http://www.realclearmarkets.com/news/reuters/finance_business/2011/Jan/20/rajaratnam_wins_ruling_wiretap_turnover_on_hold.html).

30. See generally Indictment, *supra* note 29.

31. *Id.* at 34 (seeking forfeiture “of at least \$20.8 million”). A superseding indictment brought in February 2010 added charges against Rajaratnam and Chiesi based upon statements made during guilty pleas of other defendants between January 7, 2010 and February 8, 2010. Press Release, U.S. Attorney S. Dist. N.Y., Manhattan U.S. Attorney Files Additional Charges Against Raj Rajaratnam and Danielle Chiesi (Feb. 9, 2010), available at <http://www.justice.gov/usao/nys/pressreleases/February10/rajaratnametals1indictmentpr.pdf>. In the main, the additional charges detailed allegedly illegal trading in more companies, while also elaborating on Rajaratnam’s “corrupt agreements” with more defendants. *Id.* At trial, the government would allege illicit profits exceeding \$72 million. Mark Hamblett, *11-Year Term for Rajaratnam Falls Short of Government Wishes*, N.Y. L.J., Oct. 14, 2011, at 1.

the Indictment also alleged violations of Rule 10b5-2,<sup>32</sup> a more modern prohibition self-explained as providing “a non-exclusive definition of circumstances in which a person has a duty of trust or confidence for purposes of the ‘misappropriation’ theory of insider trading.”<sup>33</sup> Within days of the Indictment, Galleon—which held approximately \$3.7 billion in assets—closed, and its investors began receiving redemptions of their investments.<sup>34</sup>

### B. *The Wiretap Battle*

A key difference between the underlying SEC and DOJ investigations lay in wiretaps, a tool routinely used by criminal investigators.<sup>35</sup> The DOJ received authority to tap Rajaratnam’s phones from March 2008 through October 2009;<sup>36</sup> the SEC, which interviewed the hedge fund titan on several occasions in the years 2007 to 2009, was precluded by law from even knowing of the wiretaps’ existence.<sup>37</sup> As the parallel matters proceeded towards separate trials, it became evident that both the civil and criminal cases would rely in part on wiretapped conversations, a first in the Commission’s storied war on insider trading.<sup>38</sup> In a written decision from February 2010 (“Rakoff Order”), District Court Judge Jed S. Rakoff, while acknowledging that the DOJ and the Commission were “partner[s]” in the Galleon investigation, noted that the two government units had not directly shared the wiretap tapes.<sup>39</sup> Based upon a joint defense agreement between certain of the Galleon Defendants (and the discovery rule codified in the Federal Rules

32. 17 C.F.R. § 240.10b5-2 (2011); *see generally* Indictment, *supra* note 29.

33. 17 C.F.R. § 240.10b5-2.

34. Michael J. de la Merced & Zachery Kouwe, *Galleon to Begin Winding Down Funds*, DEALBOOK (Oct. 21, 2009, 12:03 PM), <http://dealbook.nytimes.com/2009/10/21/galleon-to-wind-down-funds/>.

35. *See* Packer, *supra* note 17, at 47–48.

36. *Id.* at 47.

37. *Id.* at 48.

38. Lattman, *supra* note 3 (noting the government’s “novel ideas and hardball tactics”). However, the tactic of playing revealing audiotapes in Manhattan securities fraud trials is not completely new. In 1989, then U.S. Attorney Rudolph Giuliani spearheaded a case that resulted in a jury convicting five executives of the firm of Princeton/Newport Partners for stock manipulation; the tapes, which were routinely kept on the trading desk of the defunct firm, provided colorful banter highlighted by one trader’s comment to another about entering “the world of . . . sleaze.” *Welcome to the World of Sleaze*, TIME, Aug. 14, 1989, at 52 (internal quotation marks omitted); *A Biography of Mayor Rudolph W. Giuliani*, NYC.GOV, <http://www.nyc.gov/html/records/rwg/html/bio.html> (last visited Apr. 20, 2012). On appeal, the convictions were vacated and a new trial ordered. *Convictions in the ‘80s, Reversals in the ‘90s*, L.A. TIMES, July 13, 1991, at D2.

39. SEC v. Galleon Mgmt., LP, 683 F. Supp. 316, 317 (S.D.N.Y. 2010) (internal quotation marks omitted).

of Civil Procedure<sup>40</sup>), Judge Rakoff ordered the defendants who had received copies of the tapes from the DOJ to, in turn, share the same with the SEC.<sup>41</sup> An immediate appeal of that ruling resulted in a temporary stay of the order to defendants to turn over the tapes.<sup>42</sup> The Rakoff Order was subsequently vacated by a panel of the Second Circuit on September 29, 2010,<sup>43</sup> striking the balance in favor of third parties:

While the SEC has a right of access to the wiretap materials, that right must be balanced against the strong privacy interests at stake in connection with the fruits of electronic surveillance. The privacy interests in the instant case merit particular attention given that the [Rakoff] disclosure order implicated thousands of conversations of hundreds of innocent parties, and that the district court ordered disclosure prior to any ruling on the legality of the interceptions and without limiting the disclosure to relevant conversations.<sup>44</sup>

Finally, on November 24, 2010, Judge Richard J. Holwell decided that the DOJ wiretaps had been lawfully obtained, freeing the evidence for submission at the scheduled criminal trial of Rajaratnam and Chiesi.<sup>45</sup>

### *C. The Rejected/Resisted Requests for Stay*

Separately, the Southern District of New York courts made their mark on procedure in other ways. Although SEC civil cases are traditionally stayed pending resolution of related criminal matters,<sup>46</sup>

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40. FED. R. CIV. P. 26(b)(1).

41. *Galleon Mgmt.*, 683 F. Supp. at 318-19. See also Zachery Kouwe, *Judge Orders Galleon Defendants to Release Tapes*, N.Y. TIMES, Feb. 10, 2010, at B2. Judge Rakoff, a former Assistant U.S. Attorney (and chief of its Business and Securities Fraud Prosecutions Unit) has in recent years openly criticized SEC settlement practices. See Luke McGrath, *Judicial Profile: Hon. Jed S. Rakoff*, FED. LAW., June 2010, at 32, 32; Mark Hamblett, *Judge Orders Hearing, Lays Out Questions for SEC over Proposed Settlement with Citigroup Global*, N.Y. L.J., Oct. 28, 2011, at 1 (noting Judge Rakoff's initial rejection of a proposed settlement between the SEC and Bank of America in September 2009); Mark Hamblett, *Judge Spurns SEC-Citigroup Deal as Contrary to Interest in Truth*, N.Y. L.J., Nov. 29, 2011, at 1 (describing rejection of a proposed \$285 million settlement as "privately negotiated on the basis of unknown facts").

42. McCool, *supra* note 29.

43. SEC v. Rajaratnam, 622 F.3d 159, 188 (2d Cir. 2010). See also *Galleon Founder Wins Stay of Wiretaps in Civil Case*, BREAKING LEGAL NEWS (Mar. 24, 2010, 10:09), <http://www.breakinglegalnews.com/entry/Galleon-founder-wins-stay-of-wiretaps-in-civil-case>.

44. *Rajaratnam*, 622 F.3d at 184.

45. Patricia Hurtado, *SEC Seeks Wiretaps from Rajaratnam for Civil Case After Judge Admits Them*, BLOOMBERG (Dec. 20, 2010, 3:02 PM ET), <http://www.bloomberg.com/news/2010-12-20/sec-seeks-wiretaps-from-rajaratnam-for-civil-case-after-judge-admits-them.html>.

46. See Donald A. Corbett & Elliott Z. Stein, *The Perils of Partial Stays in Parallel Proceedings*, N.Y. L.J., May 7, 2010, at 4 ("Generally, in a parallel civil litigation where the plaintiff is a government agency, courts are more likely to find that the defendant is burdened, and are therefore more likely to stay the civil case.").



Judge Rakoff refused to slavishly follow the pattern, initially setting the trial date on the 2009 SEC Complaint for August 2010.<sup>47</sup> In September 2010, as the Second Circuit announced in vacating the Rakoff Order, the SEC trial remained scheduled for February 2011.<sup>48</sup> Meanwhile, the DOJ took the initiative in announcing that the SEC would no longer robotically stay its own actions in abeyance of a parallel criminal proceeding.<sup>49</sup> And even after the lack of an adjournment had been loudly chastised by the appellate court, Judge Rakoff, in June 2011, refused to delay the start of the civil trial until after sentencing (which had been set for August 2011).<sup>50</sup>

#### D. The Criminal Trial

Thus, amidst a resolved battle over the wiretaps and an unresolved one about civil stays, the criminal trial against Rajaratnam commenced in March 2011 in lower Manhattan.<sup>51</sup> The federal prosecutors were described as very confident.<sup>52</sup> The prosecution's case, which relied in

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47. See Erin Geiger Smith, *Summer SEC Trial for Raj Rajaratnam*, BUS. INSIDER LAW REVIEW (Nov. 4, 2009), [http://articles.businessinsider.com/2009-11-04/law\\_review/29983912\\_1\\_trial-date-sec-complaint-hearing](http://articles.businessinsider.com/2009-11-04/law_review/29983912_1_trial-date-sec-complaint-hearing).

48. *Rajaratnam*, 622 F.3d at 166-67, 188. The Second Circuit noted that the U.S. Attorney's office had unsuccessfully "intervened and moved to adjourn the civil trial until after the completion of the criminal trial." *Id.* at 166. The court's words were both direct in revealing sentiments and telling in revealing triage strategies:

The more prudent course in the instant case may have been to adjourn the civil trial until after the criminal trial. Apparently, all the parties agreed to such a request, yet the district court declined to grant it. Were the civil trial adjourned, the most relevant wiretapped conversations, assuming they were found to be legally intercepted, might well be publicly disclosed at the criminal trial, and the SEC would then be able to use these materials in a civil proceeding without implicating any weighty privacy rights. Such an adjournment would have the added benefit of making the district court's job of balancing any relevant interests significantly easier.

*Id.* at 186.

49. Bruce Carton, *SEC Won't Always Stay Its Proceedings for DOJ Cases*, COMPLIANCE WK. (May 4, 2010), <http://www.complianceweek.com/sec-wont-always-stay-its-proceedings-for-doj-cases/article/188270/> (quoting a DOJ assistant attorney general as saying that "the days are gone where the civil action will necessarily be stayed until the criminal action is over" (internal quotation marks omitted)). A government spokeswoman later added that the statement had been made in response to cases in which courts had "elected not to put SEC civil cases on hold." *Id.* (internal quotation marks omitted).

50. Order at 3, *SEC v. Galleon Mgmt., LP*, 2011 WL 5374112 (S.D.N.Y. Nov. 8, 2011) (No. 09 Civ. 8811 (JSR)) (order refusing to move trial date from August 22, 2011). See Ian Thomas, *Judge Won't Delay Civil Case for Rajaratnam Sentence*, LAW360 (June 6, 2011, 5:06 PM ET), <http://www.law360.com/newyork/articles/249593> (noting that the SEC asked for the delay to adjust its disgorgement request based upon the monetary sanction (if any) to be announced at Rajaratnam's sentencing).

51. Packer, *supra* note 17, at 51.

52. Katie Benner, *Welcome to the Raj Rajaratnam Show*, CNN MONEY (Mar. 9, 2011, 9:49 AM ET), <http://finance.fortune.cnn.com/2011/03/09/welcome-to-the-raj-rajaratnam-show/> (noting

large part on cooperating co-defendants, alleged that sixteen insiders were part of various conspiracies generating nearly \$64 million in profits and victimizing at least nineteen public companies.<sup>53</sup> On the first day of trial, Anil Kumar, the prosecution's lead witness, took the stand. Kumar—Rajaratnam's source, an investor with Galleon, and a director at McKinsey—testified clearly to trading confidential information for cash from Rajaratnam.<sup>54</sup>

Subsequently, the prosecutors played forty-six wiretap tapes for the jury, who heard Kumar reduce the economic crisis to his inability “to get the percentage” on a trade, and a Galleon employee advising Chiesi to “trade around [a] position” to avoid detection by the SEC.<sup>55</sup> Rajaratnam did not take the stand, and his defense centered on the testimony of a finance professor that the importance of the obtained inside information was minimized by the amount of publicly available information in the marketplace.<sup>56</sup> Additionally, the defense offered the testimony of Galleon's head of research and an array of public reports and articles to portray the defendant as a diligent student of the market.<sup>57</sup>

In summation, the prosecutor belittled diversionary tactics by the defense, which was characterized as asking the jury to “ignore logic, forget reality and suspend common sense.”<sup>58</sup> In turn, the defense, in

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that “19 people [had] already pled guilty in the vast, ongoing insider trading bust” and quoting an attorney for a former Galleon employee as being “surprised” that his client's testimony was deemed unnecessary, concluding that the government “must be very confident” (internal quotation marks omitted)).

53. Hamblett, *supra* note 31, at 6; Packer, *supra* note 17, at 51.

54. Packer, *supra* note 17, at 51-52. The exchange between the prosecutor and Kumar was hauntingly confessing:

**PROSECUTOR:** “At the very beginning, . . . you thought he was asking for legitimate information?”

**KUMAR:** “Yes, sir.”

**PROSECUTOR:** “And, once he started paying you, he was asking you for confidential information?”

**KUMAR:** “That's correct, sir.”

**PROSECUTOR:** “And, once he was paying you, you started giving it to him?”

**KUMAR:** “Yes, that is correct, sir. To my eternal regret.”

*Id.* at 52 (internal quotation marks omitted). Kumar was paid \$2.1 million by Rajaratnam for information. *Id.* at 51. Other co-conspirators confessed via their entries of pleas; one of the last to do so was Chiesi, who admitted to bringing “disrepute to what is an honorable profession.” *Id.*

55. *Id.* at 53, 55.

56. *Id.* at 53; Peter J. Henning, *Don't Fight the Wiretaps*, DEALBOOK (June 21, 2011, 3:27 PM), <http://dealbook.nytimes.com/2011/06/21/dont-fight-the-wiretaps/>.

57. Azam Ahmed, *Defense in Insider Trial Seeks to Present Galleon as Disciplined*, DEALBOOK (Apr. 11, 2011, 9:15 PM), <http://dealbook.nytimes.com/2011/04/11/rajaratnam-lawyers-open-defense/>.

58. Azam Ahmed & Peter Lattman, *Jury Deliberation Begins at Insider Trading Trial*, N.Y. TIMES, Apr. 26, 2011, at B2.

effect, argued that a surplus of information in and about the modern marketplace prevented information from ever being secret.<sup>59</sup> The judge's ensuing jury instructions were said to have been thorough, providing "lengthy legal definitions for everything from reasonable doubt to conspiracy."<sup>60</sup> On the question of what degree of reliance on the inside information need be shown, the judge's instructions told the jury that it would need to be "persuaded beyond a reasonable doubt that material nonpublic information given to the defendant was a factor, however small, in the defendant's decision to purchase or sell stock."<sup>61</sup>

Approximately eight weeks after commencing, the criminal trial went to the jury in late April 2011.<sup>62</sup> After twelve days of deliberations, Rajaratnam was found guilty of all fourteen counts.<sup>63</sup> The court then entertained rival sentencing memoranda, which—perhaps predictably—centered on the dangers posed by insider trading.<sup>64</sup> While the Sentencing Recommendation recommended a fifteen-year sentence,<sup>65</sup> prosecutors sought a criminal sentence in the range of nineteen and a half to twenty-four and a half years, citing the "significant danger that these executives and money managers may view a light sentence as an insufficient deterrent to insider trading."<sup>66</sup> Conversely, the defense argued in favor of a range under three years, commensurate with the sentences meted out to several co-conspirators who had entered guilty pleas.<sup>67</sup> The defense's filing attempted to distinguish the insider trader from the blatant thief, arguing that "a defendant tippee who profits from illegal trading does not engage in conduct that is as culpable as a defendant who affirmatively steals the same amount from an identifiable victim."<sup>68</sup>

On October 13, 2011, the trial judge sentenced Rajaratnam to eleven years in prison—a term the press noted was "substantially below the range recommended by the federal guidelines"<sup>69</sup> (as well as the range

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59. Packer, *supra* note 17, at 52.

60. Ahmed & Lattman, *supra* note 58.

61. Charge to the Jury at 49, *United States v. Rajaratnam*, No. S2 09 Cr. 1184 (RJH) (S.D.N.Y. Apr. 25, 2011).

62. Peter J. Henning, *The Crucial Question for the Rajaratnam Jury*, DEALBOOK (Apr. 25, 2011, 10:05 AM), <http://dealbook.nytimes.com/2011/04/25/the-key-question-for-the-rajaratnam-jury/>.

63. Packer, *supra* note 17, at 54.

64. See Henning, *supra* note 3.

65. Sentencing Recommendation at 57, *United States v. Rajaratnam*, No. S2 09 CR 1184-01 (RJH) (S.D.N.Y. Nov. 1, 2011).

66. Henning, *supra* note 3 (internal quotation marks omitted).

67. *Id.*

68. *Id.* (internal quotation marks omitted).

69. Peter J. Henning, *The Road Ahead for Raj Rajaratnam*, DEALBOOK (Oct. 14, 2011, 8:22 AM), <http://dealbook.nytimes.com/2011/10/14/the-road-ahead-for-raj-rajaratnam/>.

requested by the prosecution).<sup>70</sup> The judge concurrently imposed fines and restitution exceeding \$63 million.<sup>71</sup> While noting the defendant's ill health, the jurist stated, "[i]nsider trading is an assault on the free markets."<sup>72</sup> The U.S. Attorney declared, "[w]e can only hope that this case will be the wake-up call we said it should be when Mr. Rajaratnam was arrested."<sup>73</sup> The defense was said to be considering an appeal based upon the government's applications for the wiretaps (and their ensuing use at trial).<sup>74</sup>

### *E. Epilogue?*

Meanwhile, the SEC trial remained set for December 5, 2011.<sup>75</sup> In October 2011, Judge Rakoff received a motion from the Commission seeking partial summary judgment ("Summary Judgment Motion") on the issue of Rajaratnam's culpability in trading on inside information in five stocks that formed part of the proof of the criminal trial.<sup>76</sup> The Summary Judgment Motion requested that, in addition to the forfeiture and fine ordered in the criminal sentencing, Rajaratnam pay a disgorgement of \$41.3 million and, pursuant to Section 21A of the Exchange Act, a civil fine exceeding \$90 million.<sup>77</sup> In opposing the motion, Rajaratnam did not contest liability (or the imposition of an SEC injunction); however, he argued that his criminal forfeiture offset any civil disgorgement, and that the fine sought by the Commission was "exorbitant" in light of his eleven-year prison sentence.<sup>78</sup>

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70. Lattman, *supra* note 3.

71. *Id.*

72. *Id.* (internal quotation marks omitted).

73. Grant McCool, *Rajaratnam Gets 11-Year Prison Sentence*, REUTERS (Oct. 13, 2011, 7:09 PM EDT), <http://www.reuters.com/article/2011/10/13/us-galleon-rajaratnam-idUSTRE79C0MC20111013?i=4> (internal quotation marks omitted).

74. Henning, *supra* note 56.

75. Order at 2, SEC v. Galleon Mgmt., LP, No. 09 Civ. 8811 (JSR) (S.D.N.Y. Feb. 3, 2011) (order setting forth the schedule for further proceedings).

76. *Rajaratnam Opposes SEC Bid for Penalties over and Above Sanctions in Criminal Case*, 43 Sec. Reg. & L. Rep. (BNA) 2156 (Oct. 24, 2011). The SEC had sought partial summary judgment on the claims in the 2009 Complaint based upon trades in five securities noted in both the civil and criminal charges. *Id.* In response, Rajaratnam argued that he had been "adequately punished" by the sanctions imposed at the end of the criminal trial. *Id.* (internal quotation marks omitted). Concurrently, the corporate defendant Galleon—which was represented by separate counsel—argued against the motion, alleging that, because it was not a party to the criminal case, it was not subject to collateral estoppel. *Id.*

77. Securities Exchange Act of 1934 § 21A(a)(1)–(2), 15 U.S.C. § 78u-1(a)(1)–(2) (2006); *Rajaratnam Opposes SEC Bid for Penalties over and Above Sanctions in Criminal Case*, *supra* note 76, at 2156.

78. *Id.* ("In light of all the factors Judge [Richard Holwell of the criminal court] carefully considered, and the substantial penalty he imposed, Mr. Rajaratnam submits that no further

On November 8, 2011, Judge Rakoff issued a brief decision imposing a civil fine of \$92,805,705 against Rajaratnam.<sup>79</sup> The opinion and order, while avoiding discussion of double jeopardy concerns, explained the court's authority to impose the maximum penalty permitted under Section 21A, as demonstrated by Second Circuit case law.<sup>80</sup> Noting that the SEC had dropped its request for disgorgement in light of the criminal forfeiture, Judge Rakoff commented that the defendant's positions "misapprehend[ed] both the nature of this parallel proceeding and the purpose[] of civil penalties."<sup>81</sup> In tersely characterizing criminal sentences with a "monetary aspect[]" as "designed to compensate victims and deprive the defendant of his ill-gotten gains," the jurist described SEC penalties as ensuring that the violator pays "'severely in monetary terms.'"<sup>82</sup> In early December 2011, Rajaratnam filed a notice with the court announcing his intention to appeal the SEC's civil penalty.<sup>83</sup>

As 2011 concluded, government enforcement efforts seemingly remained focused on white collar insider trading, particularly, attorney defendants<sup>84</sup> and hedge fund advisers.<sup>85</sup> Rajaratnam had lost his bid to avoid double penalties from the government.<sup>86</sup> Separately, Rajav Gupta, a friend and source to Rajaratnam, was alleged to have tipped Rajaratnam on at least one stock and was named in both SEC and criminal charges on October 26, 2011.<sup>87</sup> This SEC complaint joined

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punishment or penalty is warranted." (internal quotation marks omitted)).

79. SEC v. Rajaratnam, No. 09 Civ. 8811(JSR), 2011 WL 5374112, at \*4 (S.D.N.Y. Nov. 8, 2011).

80. *Id.* at \*1-2.

81. *Id.*

82. *Id.* at \*2. Judge Rakoff added that "this case cries out for the kind of civil penalty that will deprive this defendant of a material part of his fortune." *Id.*

83. Chad Bray, *Rajaratnam May Appeal Record SEC Penalty*, WALL ST. J. L. BLOG (Dec. 7, 2011, 3:43 PM), <http://blogs.wsj.com/law/2011/12/07/rajaratnam-may-appeal-record-sec-penalty/>.

84. See, e.g., *Two Attorneys Settle SEC Insider Trading Charges*, 43 SEC. REG. & L. REP. (BNA) 2160 (Oct. 24, 2011).

85. Benton Campbell & Maria Barton, *SEC Targets Fund Advisors*, N.Y. L.J., Nov. 7, 2011, at 9 (detailing the work of the Commission's Asset Management Unit as "the largest of five specialized units created during the [Division of Enforcement's] recent restructuring"); Peter Lattman, *New Round of Insider Trading Charges Is Expected*, DEALBOOK (Nov. 30, 2011, 11:32 PM), <http://dealbook.nytimes.com/2011/11/30/new-round-of-insider-trading-charges-expected/> (disclosing the "expected" charges resulting from FBI raids of two hedge funds in 2010).

86. See *Rajaratnam Opposes SEC Bid for Penalties over and Above Sanctions in Criminal Case*, *supra* note 76, at 2156.

87. Press Release, U.S. Sec. & Exch. Comm'n, SEC Files Insider Trading Charges Against Rajat Gupta (Oct. 26, 2011), <http://www.sec.gov/news/press/2011/2011-223.htm>. The more recent SEC Complaint focuses on alleged tips from Gupta concerning the stock of Goldman Sachs. *Id.* This case is set for trial in the Southern District of New York in May 2012. See Patricia Hurtado, *Gupta Wasn't Rajaratnam's Only Goldman 'Insider,' U.S. Says*, BLOOMBERG (Feb. 8, 2012),

Rajaratnam as a defendant, marking the fourth government charging instrument against the hedge fund king within two years.<sup>88</sup>

On November 30, 2011, Rajaratnam asked the U.S. Court of Appeals for the Second Circuit to reverse a prior denial of bail and free him until the appeal of the criminal trial verdict.<sup>89</sup> The defendant argued that the government's request for the wiretaps misled the approving judge, thus rendering the tapes inadmissible at Rajaratnam's trial.<sup>90</sup> One day later, the Second Circuit denied the request via a one-line opinion; Rajaratnam's appeal of his conviction in the criminal trial is set for 2012.<sup>91</sup>

### III. WHAT HAS CHANGED, PROCEDURALLY AND SUBSTANTIVELY

On the surface, the Rajaratnam conviction presents an immediate change to securities fraud detection and punishment. To be sure, the use of criminal investigative tactics in an insider trading case dramatically heightens the crime and its pursuit.<sup>92</sup> Likewise, the eleven-year sentence punctuates a period of unprecedented incarceration: since 2009, the federal courts in New York have sent convicted insider traders to jail seventy-nine percent of the time (up from fifty-nine percent in the 2000s, and somewhere under fifty percent in the decade before).<sup>93</sup> Likewise, the median sentence for those so incarcerated has risen to approximately two and a half years (as opposed to eighteen months in the prior decade and eleven and a half months between 1993 and 1999).<sup>94</sup>

But the SEC's proclivity towards deputizing the deputies raises a host of problems. The conflicts posed by the indirect sharing of evidence (and headline-grabbing partitioning of results) may forestall certainty in both enforcement theory and individual outcomes. Witness the words of Judge Rakoff's Order of February 2010:

More broadly, the notion that only one party to a litigation should have access to some of the most important non-privileged evidence bearing

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<http://www.bloomberg.com/news/2012-02-07/ex-goldman-sachs-director-gupta-s-trial-set-for-may-after-new-arraignment.html>.

88. *Id.* Rajaratnam's participation in this additional SEC case was effectively ended via his settlement with the Commission in November 2011. *See supra* note 79 and accompanying text.

89. Mark Hamblett, *Rajaratnam to Begin Prison Sentence on Monday*, N.Y. L.J., Dec. 2, 2011, at 1.

90. *See id.*

91. *Id.*

92. *See* Brotman & Dougherty, *supra* note 12, at 16-19.

93. Chad Bray & Rob Barry, *Long Jail Terms on Rise: Inside Trades Draw Lengthier Sentences, Analysis Finds; Rajaratnam Penalty Today*, WALL ST. J., Oct. 13, 2011, at C1 (noting the findings of a *Wall Street Journal* analysis).

94. *Id.*

directly on the case runs counter to basic principles of civil discovery in an adversary system and therefore should not readily be inferred, at least not when the party otherwise left in ignorance is a government agency charged with civilly enforcing the very same provisions that are the subject of the parallel criminal cases arising from the same transactions.<sup>95</sup>

Overall, in terms of both procedure and substantive law, the fights on all fronts are bound to have precedential consequences.<sup>96</sup>

#### A. *On Criminal Referrals and Procedure . . .*

Concerning SEC referrals to other authorities, practitioners and commentators alike have grappled with the threshold for “criminal” securities fraud. While Section 21(d) of the Exchange Act clearly contemplates referrals from the Commission to the DOJ,<sup>97</sup> the factors prompting such referral have, at best, been kept vague and, at worst, been subject to public perceptions and attendant pressures.<sup>98</sup> Moreover, the typical SEC civil case enjoys such luxuries as a lower pleading burden,<sup>99</sup> near freedom from statutes of limitations (“SOL”),<sup>100</sup> and

95. SEC v. Galleon Mgmt., LP, 683 F. Supp. 2d 316, 318 (S.D.N.Y. 2010).

96. See Peter Lattman, *Insider Case May Consult President of Goldman*, N.Y. TIMES, Nov. 19, 2011, at B6 (noting that, at a court hearing the day before, lawyers for one of Rajaratnam’s alleged tippers and federal prosecutors “debated the timing of depositions that are set to be taken in a parallel [SEC] civil case”).

97. Securities Exchange Act of 1934 § 21(d), 15 U.S.C. § 78u(d)(1) (2006) (“The Commission may transmit such evidence as may be available concerning such acts or practices as may constitute a violation of any provision of this chapter or the rules or regulations thereunder to the Attorney General, who may, in his discretion, institute the necessary criminal proceedings under this chapter.”).

98. See Douglas Rappaport et al., *When Is Insider Trading Subject to Criminal Prosecution?*, N.Y. L.J., July 7, 2008, at 10.

99. *Steadman v. SEC*, 450 U.S. 91, 95-96 (1981) (setting forth a preponderance of the evidence standard of proof).

100. The securities laws are silent on the applicability of any SOL to SEC enforcement actions. JAMES D. COX ET AL., *SECURITIES REGULATION: CASES AND MATERIALS* 609 (6th ed. 2009). Concurrently, the traditional view is that the defense of laches “is not available in either SEC enforcement actions or government criminal actions.” *Id.* at 802. In 1991, the U.S. Supreme Court applied a statutory one year SOL from the date of discovery/three year maximum SOL governing private actions based upon misleading initial public offering registration materials. *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 501 U.S. 350, 353-55, 364 (1991) (applying the express provisions of § 13 of the Securities Act). That construct was extended to two years/five years in 2002 by Section 804 of the Sarbanes-Oxley Act for actions alleging “fraud.” Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 804, 116 Stat. 801 (codified at 28 U.S.C. § 1658 (2006)). In recent years, a number of federal courts have ruled that the generic SOL holding governmental actions for fines and penalties to five years applies to SEC actions seeking civil fines, but not to SEC actions seeking disgorgement or rescission. See, e.g., *SEC v. Jones*, 476 F. Supp. 2d 374, 380-83, 385 (S.D.N.Y. 2007) (dismissing the Commission’s claim for civil penalties as time barred by 28 U.S.C. § 2462).

limitless references to the accused's assertion of the Fifth Amendment privilege from self-incrimination.<sup>101</sup>

Additionally, the furthering of insider trading case law through criminal actions is of marginal value to future SEC actions. It is axiomatic that the use of such criminal precedent poses new pleading obstacles to the SEC. First and foremost, it is not inconceivable that a future defendant facing parallel civil and criminal actions will successfully invoke the U.S. Constitution's double jeopardy clause.<sup>102</sup> Between 1989 and 1997, there loomed the specter that a civil action brought by the government could seek penalties so punitive and/or redundant as to constitute an impermissible criminal action.<sup>103</sup> Pursuant to this view under *United States v. Halper*,<sup>104</sup> the SEC ran the risk of its fines imposed after criminal convictions being evaluated for constitutionality.<sup>105</sup> The concern was more than just theoretical.<sup>106</sup>

Subsequently, in *Hudson v. United States*,<sup>107</sup> the U.S. Supreme Court modified the standard to preclude only truly "criminal" subsequent punishment, while encouraging an analysis that deferred to congressional labeling of a penalty as civil in nature.<sup>108</sup> *Hudson* further educated that such statutory analysis involves a two-part scrutiny of, in turn, (1) whether the effecting legislature "indicated either expressly or impliedly a preference for one label or the other," and (2) "whether the statutory scheme was so punitive either in purpose or effect."<sup>109</sup> The *Hudson* Court added that, in determining whether a civil penalty could

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101. See Audrey Strauss, *Recent Insider Trading Jury Charges: 'Possession' vs. 'Use,'* N.Y. L.J., July 7, 2011, at 5, 7 (noting the Commission's entitlement to "an adverse inference from the defendants' invocation of Fifth Amendment rights").

102. U.S. CONST. amend. V.

103. See, e.g., *United States v. Halper*, 490 U.S. 435, 449-50, 454 (1989) (finding that imposed fines bore no "rational relation" to the harm caused by the defendant and thus constituted a second criminal sanction).

104. 490 U.S. 435 (1989).

105. See Matthew Scott Morris, Comment, *The Securities Enforcement Remedies and Penny Stock Reform Act of 1990: By Keeping Up with the Joneses, the SEC's Enforcement Arsenal is Modernized*, 7 ADMIN. L.J. AM. U. 151, 182 (1993) (citations omitted) (noting that "punitive monetary penalties only raise double jeopardy concerns when multiple sanctions are consecutively levied for a single securities infraction").

106. See, e.g., *United States v. Stoller*, 78 F.3d 710, 713, 724 (1st Cir. 1996) (evaluating a Federal Deposit Insurance Corporation debarment proceeding against a bank CEO and holding that it did not violate double jeopardy because the agency action was "predominantly remedial in nature").

107. 522 U.S. 93 (1997).

108. *Id.* at 102-04.

109. *Id.* at 99 (internal quotation marks omitted) (citing *United States v. Ward*, 448 U.S. 242, 248-49 (1980); *Rex Trailer Co. v. United States*, 350 U.S. 148, 154 (1956)). The *Hudson* Court detailed seven "useful guideposts" for part two of the analysis. *Id.* at 99-100 (citing *Kennedy v. Mendoza-Martinez*, 372 U.S. 144, 168-69 (1963)).



be declared criminal, only the “clearest proof [would] suffice.”<sup>110</sup> In essence, *Hudson* replaced the “overwhelmingly disproportionate” analysis of *Halper* with one of statutory intent.<sup>111</sup>

Shortly thereafter, the SEC benefitted from the Second Circuit’s *SEC v. Palmisano*<sup>112</sup> decision, which—specifically regarding Section 21A<sup>113</sup>—upheld the imposition of a \$9.2 million disgorgement and a \$500,000 civil fine following a criminal conviction (wherein the defendant had been ordered to pay unspecified restitution).<sup>114</sup>

But the Commission, by openly seeking disgorgement and the statutory maximum in civil fines against Rajaratnam, perhaps pressed its luck. Post-conviction, but on the eve of civil trial, Rajaratnam asked the court to preclude such a penalty on double jeopardy grounds.<sup>115</sup> He failed, both in getting the SEC fine reduced and in prompting Judge Rakoff to undertake a double jeopardy analysis in his decision.<sup>116</sup> While the ruling of Judge Rakoff may simply reiterate the Second Circuit’s support for evaluating a broad array of factors in imposing maximum treble fines under Section 21A,<sup>117</sup> the jurist refused to even entertain the notion that the SEC fine—coming on the immediate heels of the criminal action—could be seen as excessive.<sup>118</sup>

For now the result is clear. In the Second Circuit, the SEC need not fear anything more than supportive analysis of its civil fines, regardless of the second level of scrutiny suggested by *Hudson*. Moreover, if Judge Rakoff’s summary judgment ruling is any indication, ancillary considerations such as the reduction of an SEC monetary fine linked to the closing of the defendant’s business<sup>119</sup> and the argument that tippees

110. *Id.* at 100 (quoting *Ward*, 448 U.S. at 249) (internal quotation marks omitted).

111. *See id.* at 100-05 (internal quotation marks omitted).

112. 135 F.3d 860 (2d Cir. 1998).

113. Section 21A permits the SEC to seek a fine up to three times the profit gained/loss avoided by the insider trader as “determined by the court in light of the facts and circumstances.” Securities Exchange Act of 1934 § 21A(a)(3), 15 U.S.C. § 78u-1(a)(3) (2006).

114. *Palmisano*, 135 F.3d at 863, 867.

115. *See Rajaratnam Opposes SEC Bid for Penalties Over and Above Sanctions in Criminal Case*, *supra* note 76, at 2156 (describing Rajaratnam’s response to the SEC’s October 2011 motion for partial summary judgment, which calculated the potential monies sought by the SEC fines as topping \$94 million).

116. *See SEC v. Rajaratnam*, No. 09 Civ. 8811(JSR), 2011 WL 5374112, at \*1, \*4 (S.D.N.Y. Nov. 8, 2011).

117. *See, e.g., SEC v. Blue Bottle Ltd.*, No. 07-CV-1380 (CSH) ESF, 2007 U.S. Dist. LEXIS 95992, at \*21-22 (S.D.N.Y. Apr. 24, 2007) (“The elements to consider in determining the penalty include, among other things, a defendant’s culpability, the amount of profits gained, and the repetitive nature of the unlawful act and the deterrent effect of a penalty given the defendant’s net worth.”).

118. *See generally Rajaratnam*, No. 09 Civ. 8811(JSR), 2011 WL 5374112.

119. *See SEC v. Pardue*, 367 F. Supp. 2d 773, 776-78 (E.D. Pa. 2005) (denying the injunction requested by the Commission and lowering its monetary penalty).

warrant less discipline than those who steal the inside information<sup>120</sup> will not garner much attention in the Second Circuit.

Practically speaking, future reliance on wiretaps, other DOJ tools, or DOJ partnering in general presages certain appeals and uncertain rulings. Complicating matters in the Rajaratnam case is the fact that, while a circuit court may soon receive an appeal, a healthy dose of the content and tenor of the Galleon wiretap evidence has already been made public.<sup>121</sup> Indeed, the imminent legal battles over the use of third party tapes in insider trading trials is at oddly hypothetical yet strangely mooted by the perceptions already solidified.

Strategically, the Rajaratnam case represents a potentially dangerous view that incarceration generally deters insider trading; the persistence of the crime in the wake of thirty years of criminal trials proves otherwise.<sup>122</sup> Despite his successes in the Galleon cases, the U.S. Attorney for the Southern District of New York earlier this year asked the U.S. Sentencing Commission for an even higher sentencing range for insider trading.<sup>123</sup> Undoubtedly, prosecutors and jurists alike seem to now more than ever be confident that indictments will affect the storied risk-benefit analysis attending aggressive decisions on Wall Street.<sup>124</sup> The federal judge who imposed sentence on Rajaratnam went so far to state that “[h]is crimes reflect a virus in our business culture that needs to be eradicated.”<sup>125</sup>

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120. See SEC v. Grossman [1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶99,518, at 97,527-28 (S.D.N.Y. May 6, 1997), *aff'd in part, vacated in part sub nom.* SEC v. Hirshberg, 173 F.3d 846 (2d Cir. 1999) (rejecting the SEC contention that a tippee has a high degree of culpability).

121. See McCool, *supra* note 73. The McCool article discloses a taped July 2008 conversation between Chiesi and Rajaratnam on a company's earnings report as follows: “They’re gonna guide down, . . . I just got a call from my guy. I played him like a finely tuned piano.” *Id.* (internal quotation marks omitted). Separately, the appellate court hearing the appeal of the Rakoff Order noted that the U.S. Attorney’s Office “inadvertently provided the SEC with a small group of wiretap recordings that were later retracted.” SEC v. Rajaratnam, 622 F.3d 159, 165 n.1 (2d Cir. 2010). Moreover, the U.S. Attorney released select excerpts of conversations prior to the criminal trial. SEC v. Galleon Mgmt., LP, 683 F. Supp. 2d 316, 317 (S.D.N.Y. 2010) (noting that the wiretaps had “already [been] partially disclosed publicly”).

122. The first cases seeking to criminally charge insider trading by corporate “outsiders” can be said to have appeared in the 1970s. See, e.g., Chiarella v. United States, 445 U.S. 222, 224-25 (1980) (reversing the 1978 conviction of a printer—not employed by any of the companies whose stocks had been traded—who had profited from discerning the names of anonymous takeover targets described in customer documents); United States v. Newman, 664 F.2d 12, 15 (2d Cir. 1981) (upholding the indictment of a tipped investment banker who had learned of takeovers from investment banking firm employees). Notably, in the *Chiarella* case, the defendant similarly faced multiple government actions. *Chiarella*, 445 U.S. at 224-25.

123. Bray & Barry, *supra* note 93, at C2.

124. See *id.*; *supra* notes 92-94, 122-23 and accompanying text.

125. Lattman, *supra* note 3 (internal quotation marks omitted).

Nonetheless, the SEC has readily embraced burgeoning criminal investigation. As the head of the Commission's Division of Enforcement proclaimed in response to a question on the financial crisis (and long before the Rajaratnam conviction): "we are enhancing our historically close working relationship with other law enforcement authorities, including the DOJ, in order to maximize the efficient use of limited resources, as well as to deliver a united and forceful response to those who would violate the federal securities laws."<sup>126</sup>

The SEC has not only acknowledged the need to refer investigations to other authorities but also has begun to take credit for the transition.<sup>127</sup> Instead of freeing SEC resources, the more immediate result of civil and criminal government agencies sharing evidence may be duplication of efforts (and litigation). As has been aptly noted, the Rajaratnam criminal trial served as a dress rehearsal for the regulators tasked with demystifying the world of information sharing in a market now tracked in milliseconds.<sup>128</sup> While the unqualified success of the U.S. Attorney's case—in addition to making public a healthy selection of wiretap evidence—showed that juries can be made to appreciate the cloak and dagger world of modern insider trading, the greatest consequence has been more insider trading trials. Notably, within a month of Rajaratnam's sentencing, new SEC charges were filed against him and one of his alleged tipsters.<sup>129</sup>

Likewise, while criminal enforcement of the securities laws may seem provocative, a world of alternatives exists for the deterrence of insider trading. For better or for worse, insider trading actions traditionally stemmed from stock exchange inquiries.<sup>130</sup> Best situated to monitor their own trading, the exchanges still provide the most reliable real-time surveillance of the daily domestic trading activity of listed

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126. *Mortgage Fraud, Securities Fraud, and the Financial Meltdown: Prosecuting Those Responsible: Hearing Before the S. Comm. on the Judiciary*, 111th Cong. 85-86 (2009) (testimony of Robert Khuzami, Director, Division of Enforcement, U.S. Securities and Exchange Commission).

127. U.S. SEC. & EXCH. COMM'N, FY 2010 PERFORMANCE AND ACCOUNTABILITY REPORT 51-52 (2010), available at <http://www.sec.gov/about/secpar/secpar2010.pdf> (describing 492 referrals of matters "more appropriately handled by another entity or in another venue," including 139 matters referred to (unspecified) criminal authorities). Prior year data was not available for either of these statistics.

128. See David Glovin, *Rajaratnam Trial Offers U.S. Chance to 'Test Drive' Gupta Insider Evidence*, BLOOMBERG (Mar. 8, 2011, 8:30 PM ET), <http://www.bloomberg.com/news/2011-03-09/rajaratnam-trial-offers-u-s-chance-to-test-drive-gupta-insider-evidence.html> (quoting an SEC official as describing the criminal trial against Rajaratnam, a tippee, as "the flip side" of a future civil case against Gupta, a tipper).

129. Press Release, U.S. Sec. & Exch. Comm'n, *supra* note 87.

130. See generally *Overview*, NYSE EURONEXT, <http://usequities.nyx.com/regulation/nyse-regulation/overview> (last visited Apr. 20, 2012) (supplying an overview of the operations of the NYSE Regulation corporation, including monitoring of trading activity).

stocks.<sup>131</sup> More importantly, such exchanges have consistently disciplined participants (both large and small) based upon an array of violations stemming from insider trading.<sup>132</sup> While exchange-based discipline is limited to member firms and their employees, the SEC enjoys boundless jurisdiction which was actually blessed with the allocation of stronger penalties under the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”).<sup>133</sup> In short, in light of the complications of time and procedure, and the dubious value in concurrent penalties, there are alternatives available to the SEC before partnering with the DOJ.

### *B. On Insider Trading Law Itself. . .*

An interesting side note to the Rajaratnam case centers on SEC advances in pleading liberality in recent years. Specifically, Rule 10b5-1 permits the SEC—in civil actions—to plead that a defendant traded “while aware of” inside information.<sup>134</sup> This seemingly harmless semantic string was actually the deliberate attempt by the Commission about a decade ago to sidestep problems at trial occasioned by the requirement that SEC attorneys distinguish between “use” and “possession” of illegally obtained information.<sup>135</sup> While commentators have noted the possible constitutional challenge to the use of Rule 10b5-1 in criminal cases (in that it obligates the defendant to prove—in violation of the due process clause of the Fifth Amendment—that he did not use the information of which he was aware),<sup>136</sup> a possible more immediate ramification is abandonment of the SEC-friendly

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131. See *id.* (noting the storied marketplace’s “limited real-time monitoring of trading activity on the facilities of the U.S. securities exchanges”).

132. See, e.g., Decision at 1, 11, Dep’t of Enforcement v. Braff, Complaint No. 2007011937001 (FINRA May 13, 2011) (noting that NASD Rule 3050(c) “acts to prevent insider trading through its notification requirements”); NYSE, Inc., Exchange Hearing Panel Decision 89-50, at 10 (June 5, 1989), available at <http://www.nyse.com/pdfs/89-050.pdf> (accepting a Stipulation of Facts and Consent to Penalty).

133. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 925, 124 Stat. 1376, 1850 (2010) (codified as amended at 15 U.S.C. §§ 78o(b)(6)(A), 78o-4(c)(4), 78q-1(c)(4)(C), 80b-3(f) (Supp. IV 2011)) (expanding SEC powers to suspend/bar officers and directors charged under a provision relating to one type of investment entity from associating with an entity targeted by another provision).

134. Selective Disclosure and Insider Trading, Securities Act Release No. 7881, Exchange Act Release No. 43,154, Investment Company Act Release No. 24,599, [2000 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,319, at 83,676 (Aug. 15, 2000).

135. See RALPH C. FERRARA, ET AL., FERRARA ON INSIDER TRADING AND THE WALL § 2.01[5], at 2-24 (2011) (describing the rule as “intended to resolve the [*use* vs. *possession*] debate once and for all”).

136. See *id.* § 2.01[5], at 2-24.15.

provision altogether in light of the varying policies of the SEC regional offices.<sup>137</sup>

The larger effect of the criminal trial of Rajaratnam still may be upon the pivotal choice of insider trading theory itself. The sources of Rajaratnam's inside information often displayed a singular position: employee of a public company, the stock of which Galleon sought to exploit.<sup>138</sup> As such, these individuals were classic "insiders" under securities law.<sup>139</sup> As insider theory has existed since 1980:

Under the "traditional" or "classical theory" of insider trading liability, § 10(b) and Rule 10b-5 are violated when a corporate insider trades in the securities of his corporation on the basis of material, nonpublic information. Trading on such information qualifies as a "deceptive device" under § 10b, we have affirmed, because "a relationship of trust and confidence [exists] between the shareholders of a corporation and those insiders who have obtained confidential information by reason of their position with that corporation."<sup>140</sup>

Concomitantly, the SEC has consistently charged corporate insiders as having a duty to their shareholders that is breached upon the use of confidential information for personal trading gain (that is, the Rule 10b-5 violation for such party does require a "theft" of the corporate information).<sup>141</sup> Yet, the U.S. Attorney's indictments charged the corporate sources of Rajaratnam's information under the

137. Compare Complaint at 14-15, *SEC v. Stewart*, No. 03 CV 4070 (S.D.N.Y. June 4, 2003) (pleading merely Stewart's *possession* of inside information at the time of her sales), with 2009 SEC Complaint, *supra* note 16, at 15-45 (pleading the defendants' actual *use* of the inside information). At least one commentator has explained the disparate pleading as evidencing an evolving government policy of pleading the higher standard. Strauss, *supra* note 101, at 7.

138. 2009 SEC Complaint, *supra* note 16, at 3-6; Lattman, *supra* note 3.

139. *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 848 (2d Cir. 1968) (declaring Board members, officers, and employees to be insiders for purposes of Rule 10b-5).

140. *United States v. O'Hagan*, 521 U.S. 642, 651-52 (1997) (quoting *Chiarella v. United States*, 445 U.S. 222, 228 (1980)).

141. In *SEC v. Peterson*, the SEC charged that:

Clayton Peterson learned the material nonpublic information that he conveyed to Drew Peterson as a result of his service on the board of directors of Mariner [Energy, Inc.], and Clayton Peterson knew, recklessly disregarded, or should have known, that he owed a fiduciary duty, or obligation arising from a similar relationship of trust and confidence, to keep the information confidential.

Amended Complaint at 11, *SEC v. Peterson*, No. 11 Civ. 5448 (RPP) (S.D.N.Y. Oct. 21, 2011). The SEC further noted in *SEC v. Waksal* that:

At the time of the transactions and events alleged in this Complaint, Waksal was ImClone's CEO, and therefore owed a fiduciary duty to ImClone and its shareholders. As a result, Waksal had a fiduciary duty, among other things, not to trade while in possession of material non-public information and to keep material non-public information confidential.

Amended Complaint at 4, *SEC v. Waksal*, No. 02 Civ. 4407 (NRB) (S.D.N.Y. Mar. 11, 2003).

misappropriation theory.<sup>142</sup> This, in effect charged them with theft from their own company, which is more difficult to prove.<sup>143</sup>

In 1997, the U.S. Supreme Court blessed the “misappropriation theory,” the mechanism by which Rule 10b-5 is applied to individuals outside of the subject corporation who trade on inside information.<sup>144</sup> In crafting the decision that still largely defines the crime, Justice Ruth Bader Ginsburg stated the following: “[i]n lieu of premising liability on a fiduciary relationship between company insider and purchaser or seller of the company’s stock, the misappropriation theory premises liability on a fiduciary-turned-trader’s deception of those who entrusted him with access to confidential information.”<sup>145</sup>

The difference between the theories is more than just ease of proof. The U.S. Sentencing Guidelines (the “Guidelines”)<sup>146</sup> classify the defendant guilty of “classic” (that is, subject company employee) insider trading under “abuse[] . . . of [a] special trust” and impose higher penalties.<sup>147</sup> Stated otherwise, a source of inside information labeled a misappropriator may receive a lesser penalty under the Guidelines when not a member of corporate management.<sup>148</sup>

## V. CONCLUSION

*“In the end, the doctors were all in accord. They agreed they had no idea what was wrong with the soldier who saw everything twice, and they rolled him away into a room in the corridor and quarantined everyone else in the ward for fourteen days.”<sup>149</sup>*

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142. Indictment, *supra* note 29, at 4. For example, in describing the acts of “[t]he [Ali] Far Inside Sources,” as the Indictment labels them, individuals employed by public companies are said to have “misappropriated [i]nside [i]nformation in violation of . . . duties . . . owed to their respective employers and their shareholders.” *Id.*

143. Simply put, whereas classic theory begins with recognition of a duty between corporate employees and corporate shareholders, misappropriation theory must search for a commensurate obligation, at times failing at the task. *See, e.g., SEC v. Talbot*, 430 F. Supp. 2d 1029, 1061 (C.D. Cal. 2006) (finding no duty by an outside director to keep confidential news of an imminent acquisition involving third parties), *rev’d*, 530 F.3d 1085, 1094 (9th Cir. 2008) (finding a duty of “trust and confidence” where a director sits on a corporate board).

144. *O’Hagan*, 521 U.S. at 649-50 (reinstating convictions for violations of SEC Rules 14e-3 and 10b-5).

145. *Id.* at 652.

146. U.S. SENTENCING GUIDELINES MANUAL (2011).

147. *Id.* § 2B1.4. & cmt. n.1; 2 WILLIAM K.S. WANG & MARC I. STEINBERG, INSIDER TRADING § 7:2.2, at 7-33 (2d ed. 2008).

148. *See* 2 WANG & STEINBERG, *supra* note 147, § 7:2.2, at 7-33 to 7-35, 7-34 n.100 (quoting *United States v. Bennett*, 161 F.3d 171, 195-96 (3d Cir. 1998); *United States v. O’Hagan*, 139 F.3d 641, 656 (8th Cir. 1998)).

149. *HELLER*, *supra* note 1, at 178.

To be sure, the vagaries surrounding the government's insider trading program shall persist. Undefined by statute<sup>150</sup>—and still considerably less forgiving than foreign counterparts<sup>151</sup>—the prohibition driving America's unique and steadfast insider trading crusade is nonetheless occasionally portrayed as too weak.<sup>152</sup> Presently, the horizons for those pursuing insider traders perhaps may have never seemed brighter. The Second Circuit has warned against contemporaneous civil and criminal trials,<sup>153</sup> thus perpetuating civil investigations endlessly. Criminal penalties for insider trading may actually increase.<sup>154</sup> Moreover, a June 2011 U.S. Supreme Court decision narrowly interpreted the right to counsel so as to preclude applicability to administrative (that is, SEC) hearings.<sup>155</sup>

In pursuing Rajaratnam, the U.S. Attorney for the Southern District of New York hinted at evolving investigative standards for an ever-evolving crime; within days of the verdict, he was quoted as saying: "When sophisticated business people begin to adopt the methods of common criminals, we have no choice but to treat them as such."<sup>156</sup> The criminal investigation and resulting actions against the Galleon Defendants were justified. The scheme's tactics were brazen. The network was far-reaching (one of the Galleon Defendants remains at large in India).<sup>157</sup> The dollar amounts were simply astronomical. And

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150. J. Scott Colesanti, "We'll Know It When We Can't Hear It": A Call for a Non-Pornography Test Approach to Recognizing Non-Public Information, 35 HOFSTRA L. REV. 539, 540-42 (2006) (noting the lack of a definition of insider trading in the Exchange Act and the present, "largely undefined prohibition").

151. See, e.g., Wertpapierhandelsgesetz [WpHG] [German Securities Trading Act], Sept. 9, 1998, BUNDESGESETZBLATT I [BGBl. I] at 2708, last amended by Gesetz [G], June 22, 2011, BGBl. I at 1126, art. 3, § 38(1) (Ger.), translated in *Securities Trading Act (Wertpapierhandelsgesetz-WpHG)*, BUNDESANSTALT FÜR FINANZDIENSTLEISTUNGS-AUFSICHT, [http://www.bafin.de/nn\\_720786/SharedDocs/Aufsichtsrecht/EN/Gesetze/wphg\\_101119\\_en.html](http://www.bafin.de/nn_720786/SharedDocs/Aufsichtsrecht/EN/Gesetze/wphg_101119_en.html) (last visited Apr. 20, 2012) (setting a limit of five years of incarceration for statutory insiders).

152. See, e.g., MICHAEL LEWIS, THE BIG SHORT: INSIDE THE DOOMSDAY MACHINE 62 (2010) ("Even as it came to dwarf the stock market, the bond market eluded serious regulation. . . . Bond traders could exploit inside information without worrying that they would be caught."); Matthew Goldstein, *Steve Cohen Says Insider Trading Rules Are "Vague,"* REUTERS (Dec. 13, 2011, 5:56 PM EST), <http://www.reuters.com/article/2011/12/13/us-sac-cohen-deposition-idUSTRE7BC1UJ20111213> (describing a famed hedge fund CEO as testifying in a 2011 deposition that it can be a "judgment call" as to whether attractive news is inside information).

153. See *supra* note 48.

154. See *supra* text accompanying notes 92-94.

155. *Turner v. Rogers*, 131 S. Ct. 2507, 2520 (2011) (holding that the due process clause does not automatically require counsel at civil contempt proceedings in a South Carolina child support arrears case).

156. Benjamin Weiser & Peter Lattman, *U.S. Prosecutor Sends a Message to Wall Street*, N.Y. TIMES, May 13, 2011, at B1 (internal quotation marks omitted).

157. Packer, *supra* note 17, at 47, 51.

insider trading is a difficult crime to prove,<sup>158</sup> perhaps warranting the most invasive of criminal investigative tools. Consequently, after so much was expended to thwart a ring so large and corrupt, the resulting message to defendants has been shouted loud and clear.<sup>159</sup>

But well-heeled people assembling an illicit informational network is hardly something new to Wall Street, having been amply elucidated in both fact<sup>160</sup> and fiction twenty-five years ago.<sup>161</sup> The new horizons augured by Professor Roberta Karmel in 1982 and by defense counsel in 2011 may equate to exponentially increased litigation occasioned by multiple governmental agencies teaming up to target a business sector such as hedge funds.<sup>162</sup> Generally, the SEC's partnership with the DOJ may succeed foremost in creating a world where pivotal issues must be tried twice; in particular, in the case of Rajaratnam, the joint efforts have resulted in a white collar criminal reporting to jail for a minimum of ten years,<sup>163</sup> having already been ordered to pay over \$63 million to the government for a set of transactions<sup>164</sup> and another \$92 million on a subset thereof.<sup>165</sup>

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158. See Henning, *supra* note 56 (noting that, in most insider trading cases, the jury is presented circumstantial evidence and is asked "to infer that the person traded on material nonpublic information").

159. See *id.* ("[T]he government's record so far is perfect on insider trading trials in which prosecutors relied on extensive wiretap evidence and other recordings. . . . The government's victories show just how enticing that type of evidence will be for prosecutors in future cases.").

160. See generally DOUGLAS FRANTZ, LEVINE & CO.: WALL STREET'S INSIDER TRADING SCANDAL (1987) (detailing the downfall of millionaire investment banker Dennis Levine and his circle of professional sources of inside information in Manhattan).

161. See, e.g., WALL STREET (Twentieth Century Fox Film Corporation 1987) (featuring an Academy Award winning performance by lead actor Michael Douglas).

162. See Reply Brief for Defendants-Appellants Raj Rajaratnam and Danielle Chiesi at 7, SEC v. Rajaratnam, 622 F.3d 159 (2d Cir. 2010) (No. 10-462-cv(L)). See generally KARMEL, *supra* note 15. The SEC has loudly proclaimed its intention to monitor and discipline hedge funds:

Dodd-Frank has not been the only origin of regulatory change for the hedge fund industry. Separate from the agency's Dodd-Frank responsibilities, the SEC in recent years has moved forward a number of regulatory initiatives of significance to hedge funds concerning matters such as short selling; the custody of advisory client assets; investment adviser disclosures; and political contributions by certain investment advisers or so-called "pay to play."

Troy A. Paredes, Comm'r, U.S. Sec. & Exch. Comm'n, Remarks at the Symposium on "Hedge Fund Regulation and Current Developments" (June 8, 2011) (footnotes omitted) (transcript available at <http://www.sec.gov/news/speech/2011/spch060811tap.htm>). Separately, the DOJ investigation of Galleon and other hedge funds spanned four years and resulted in the (sealed) wiretaps of 655 individuals. Reply Brief for Defendants-Appellants Raj Rajaratnam and Danielle Chiesi, *supra*, at 7. The wiretaps extended to the subjects' "home, office and mobile phones." *Rajaratnam*, 622 F.3d at 165.

163. Henning, *supra* note 69.

164. Lattman, *supra* note 3.

165. *Citing Deterrent Effect, Court Imposes Record \$92M Fine on Rajaratnam*, Sec. Reg. & L. Rep. (BNA) 2297 (Nov. 14, 2011). The SEC imposed a total amount of "monetary sanctions . . . on



Accepting the blatant illegality of Rajaratnam's tactics, the more harrowing result still is that the promised complement of criminal and civil investigative efforts has arguably led primarily to more work for the under-resourced SEC. Stated bluntly, rather than supplement or lessen Commission efforts, the criminal pleas, trial, and battles over Galleon have led to more SEC complaints and duplicative penalties.<sup>166</sup> Moreover, the exacting of leviathan monies from a well-publicized tycoon has done little to quell the rage over Commission practices and acknowledged failures.<sup>167</sup> Further, the doctrine of civil stays has actually been reconstrued to permit amplified civil actions based upon criminal results: both the 2009 SEC Complaint and the 2011 SEC Complaint incorporate language generated by preceding criminal pleas and/or indictments.<sup>168</sup> Finally, the successive layering of monetary fines appears subject to the most narrow judicial scrutiny feasible, while both ignoring constitutional concerns and emphasizing the accused's lifestyle.<sup>169</sup>

In terms of the public's clamor for accountability for the ongoing financial crisis,<sup>170</sup> such double-dipping in the insider trader pool seems misplaced; in terms of the desire for a prohibition that provides clarity and deterrence,<sup>171</sup> the fighting on two fronts seems outright hazardous.

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Rajaratnam in both cases" exceeding \$156.6 million. *Id.*

166. The more frequent actions and ever-expanding fine pools do, predictably, bolster tallies necessitated by the Commission's reliance upon congressional funding. *See* Press Release, U.S. Sec. & Exch. Comm'n, SEC Enforcement Division Produces Record Results in Safeguarding Investors and Markets (Nov. 9, 2011), <http://www.sec.gov/news/press/2011/2011-234.htm> (detailing the filing of 735 enforcement actions and the imposition of over \$2.8 billion in disgorgement and penalties in fiscal year 2011).

167. *See, e.g.,* Edward Wyatt, *Promises Made, and Remade, by Firms in S.E.C. Fraud Cases*, N.Y. TIMES, Nov. 8, 2011, at A1 ("A Times analysis of [SEC] enforcement actions during the past 15 years found at least 51 cases in which the S.E.C. concluded that Wall Street firms had broken anti-fraud laws they had agreed never to breach. The 51 cases spanned 19 different firms."); *SEC Folks Slide on Madoff*, N.Y. POST (Nov. 12, 2011, 1:32 AM), [http://www.nypost.com/p/news/national/sec\\_folks\\_slide\\_on\\_madoff\\_z44DLG65xzqgd9OTgI2khK](http://www.nypost.com/p/news/national/sec_folks_slide_on_madoff_z44DLG65xzqgd9OTgI2khK) (describing the Commission's internal disciplining of seven employees based upon its collective failure "to stop Bernard Madoff's long-running investment fraud despite repeated warnings").

168. *See supra* note 27 (detailing the additional charges in the 2009 SEC Complaint inspired by the entry of criminal pleas by certain Galleon Defendants). *See also* SEC v. Galleon Mgmt., LP, 683 F. Supp. 2d 316, 317 (S.D.N.Y. 2010) (noting that the SEC and the DOJ were "in the Government's word, 'partner[s]' in the investigation of the underlying allegations"); Press Release, U.S. Sec. & Exch. Comm'n, *supra* note 87 (acknowledging the "ongoing assistance and cooperation of the U.S. Attorney's Office for the Southern District of New York and the Federal Bureau of Investigation").

169. *See, e.g.,* SEC v. Rajaratnam, No. 09 Civ. 8811(JSR), 2011 WL 5374112, at \*2 (S.D.N.Y. Nov. 8, 2011) ("[T]his case cries out for the kind of civil penalty that will deprive this defendant of a material part of his fortune.").

170. *See* Packer, *supra* note 17, at 48 (quoting award-winning filmmaker Charles Ferguson as declaring "[t]hree years after a horrific financial crisis caused by massive fraud, not a single financial executive has gone to jail, and that's wrong" (internal quotation marks omitted)).

171. In recent years, a number of key insider trading cases brought against "outsiders" have

At year end 2011, residential foreclosures continued at alarming rates,<sup>172</sup> municipalities throughout the country faced the specter of bankruptcy,<sup>173</sup> no executive had gone to jail for any role in the financial crisis,<sup>174</sup> and the public still feared unabated insider trading by Congress.<sup>175</sup> Alarming, the federal legislative response to the continuing financial crisis has been stalled by its own weight, with less than twenty-five percent of its reforms enacted over the seventeen months after its passage.<sup>176</sup> Against this backdrop of uncertainty and excused inaction, headline insider trading actions—like the visions before that famed hospital patient in *Catch-22*—are being viewed twice. Few would argue that hedge fund operators knowingly trading cash for unique advantage deserve forgiveness, but many might assert that meaningful regulation sometimes requires knowing when the battle is being aptly fought by others (and legal resources thus better allocated elsewhere).

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seen district courts and their appellate reviewers adopt diametrically opposed views on the existence of the predicate duty. *Compare* SEC v. Dorozhko, 574 F.3d 42, 49-51 (2d Cir. 2009) (remanding a Southern District of New York decision that an alleged hacker had no fiduciary duty to his corporate victim to disclose or abstain), *with* SEC v. Cuban, 620 F.3d 551, 552, 557-58 (5th Cir. 2010) (vacating and remanding a district court's finding that a client who was allegedly told of an imminent corporate private placement—which would likely devalue registered corporate shares—owed no duty to the corporation to refrain from selling).

172. Kevin Simpson, *Why Are Foreclosures Continuing if Mortgage Delinquencies Are Really Declining?*, FORECLOSURELISTINGS.COM, <http://www.foreclosurelistings.com/content/foreclosures/foreclosures-continuing-mortgage-delinquencies-declining.htm> (last visited Apr. 20, 2012) (noting a foreclosure rate of 9.13 percent despite foreclosure “freezes” in certain areas).

173. Mark Curriden, *The Next Chapter*, A.B.A. J., Nov. 2011, at 51, 52. Mr. Curriden's article describes a Northwestern University study estimating \$3 trillion in unfunded state employee pension funds, as well as \$574 billion in unfunded local municipal government pension fund liabilities. *Id.* See also Campbell Robertson et al., *Bankruptcy Rarely Offers Easy Answer for Counties*, N.Y. TIMES, Nov. 11, 2011, at A15 (noting the difficulties confronting the recent filing by Alabama's Jefferson County, “the largest municipal bankruptcy in American history”).

174. Packer, *supra* note 17, at 48.

175. See Donna M. Nagy, *Insider Trading, Congressional Officials, and Duties of Entrustment*, 91 B.U. L. REV. 1105, 1106 & nn.1, 4 (2011) (detailing *Wall Street Journal* articles in 2004 and 2010 alleging that “[c]ongressional staff are often privy to inside information” and that “senators’ uncanny ability to know when to buy or sell their shares seems to stem from having access to information that other investors wouldn’t have” (citation omitted) (internal quotation marks omitted)).

176. DAVIS POLK, DODD-FRANK PROGRESS REPORT 10 (2011), available at [http://www.davispolk.com/files/Publication/e3379fb6-ab9d-4ed8-b873-0877696a8005/Presentation/PublicationAttachment/690130be-02e6-4037-88e8-01648c94664f/November2011\\_Dodd.Frank.Progress.Report.pdf](http://www.davispolk.com/files/Publication/e3379fb6-ab9d-4ed8-b873-0877696a8005/Presentation/PublicationAttachment/690130be-02e6-4037-88e8-01648c94664f/November2011_Dodd.Frank.Progress.Report.pdf).

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