No. 20-1161

In the
Supreme Court of the United States

EDWARD J. KOSINSKI,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

REPLY IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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INTRODUCTION

For over four decades, the law has been clear: Trading on material nonpublic information is not fraudulent unless a fiduciary or similar duty of "trust *and* confidence" has been breached. As this Court has repeatedly held, the breach of such a duty is what separates innocent investment decisions from criminal insider trading. The Second Circuit's decision, however, eviscerates this critical duty requirement and radically expands insider-trading fraud liability in three important respects. First, the Second Circuit excised "trust and" from the duty of "trust and confidence" by holding that people who agree to keep information confidential must refrain from trading—even if there is no fiduciary or similar relationship, and even if they comply with their confidentiality obligation. Second, the court rejected any clear "test of fiduciary status" in favor of a case-by-case, common-law style inquiry that is inherently vague and standardless. Third, the Second Circuit held that appellate courts can affirm an insider-trading conviction on a legal theory the jury never considered, even if the jury instructions misdefined an element of the crime.

Remarkably, the government offers no substantive defense of the Second Circuit's decision. Instead, it attempts to minimize the ruling's significance and responds to straw men instead of petitioner's actual arguments. First, the government contends that petitioner "misreads" the decision below and denies the Second Circuit held that a simple confidentiality agreement can establish the requisite duty of "trust and confidence." But the Second Circuit itself agrees with petitioner's reading of its opinion; it has already said so, in *United States v. Chow*, 993 F.3d 125 (2d Cir. 2021). And the government does not dispute that if a mere confidentiality agreement suffices to establish "trust and confidence" in the Second Circuit, its rulings conflict with the law of the Fifth Circuit.

Second, as to vagueness, the government focuses on an argument petitioner did not make—that the duty of "trust and confidence" is unconstitutionally vague. That is not the issue. There is nothing vague about "trust and confidence" to the extent it covers traditional, quintessentially fiduciary and similar relationships in which the duty is "usually beyond dispute." *Skilling v. United States*, 561 U.S. 358, 407 n.41 (2010). But the Second Circuit expanded the duty to reach an indeterminate and boundless range of relationships without any fair notice *ex ante*.

Third, contrary to the government's assertion, the Second Circuit did not conclude "beyond a reasonable doubt that the error complained of did not contribute to the verdict obtained." *Neder v. United States*, 527 U.S. 1, 15 (1999). Nor could it have done so, because the jury was instructed that a confidentiality agreement necessarily created a duty of trust and confidence. The Second Circuit's approach permits appellate courts to substitute their own findings about the evidence for those of a properly-instructed jury, in violation of the Sixth Amendment and this Court's decisions.

This case epitomizes the Second Circuit's recent efforts to expand and reshape insider-trading law far beyond the bounds established by this Court. It creates significant uncertainty for market participants and undermines the need for clear rules in "an area that demands certainty and predictability." *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 188 (1994). Because the Second Circuit's decisions set the rules that govern most transactions on our nation's securities markets, it is imperative that this Court intervene.

I. This Court Should Review The Second Circuit's Ruling That A Confidentiality Agreement By Itself Establishes A Duty of "Trust And Confidence"

Citing its prior decisions, the Second Circuit unambiguously held that "an explicit acceptance of a duty of confidentiality is itself sufficient to establish the necessary fiduciary duty of trust and confidence." Pet.App.19a (quotation marks omitted); *see* Pet.App.28a (citing *United States v. Falcone*, 257 F.3d 226 (2d Cir. 2001); *United States v. Chestman*, 947 F.2d 551 (2d Cir. 1991) (en banc)). Based on that principle, the court concluded that the confidentiality clause "provided Regado with the 'trust and confidence' it required to disclose to [Kosinski] critical inside information," and rendered "Kosinski's relationship with Regado…fiduciary in nature." Pet.App.19a, 17a.

The government does not dispute that this holding contravenes this Court's decisions establishing that a fiduciary or similar duty of "*trust* and confidence" is required to establish insider-trading fraud, or that it is the duty of *trust*, not the duty of confidence, that creates an obligation to refrain from trading. *See Salman v. United States*, 137 S. Ct. 420, 423 (2016); *United States v. O'Hagan*, 521 U.S. 642, 652 (1997); *Dirks v. SEC*, 463 U.S. 646, 654 (1983); *Chiarella v. United States*, 445 U.S. 222, 230 (1980); Petition.20.

And the government concedes that the Fifth Circuit recognizes that a mere agreement to keep information confidential—without more—is insufficient. *See* BIO.11; Petition.24-25.

Accordingly, the government makes no attempt to defend the Second Circuit's holding. Instead it asserts that petitioner "misreads the court of appeals' opinion" and that there is no circuit split because the confidentiality clause had no independent significance to the Second Circuit's ruling. BIO.9, 11. The passages quoted above conclusively demonstrate the fallacy of this argument. But there is more: The Second Circuit itself has expressly refuted the government's misreading of its decision.

In *Chow*, the Second Circuit affirmed the insider-trading convictions of a similarly-situated defendant who had entered into non-disclosure agreements that, he argued, did not establish a duty of trust and confidence. The court discussed this case extensively and relied upon it to reject Chow's arguments as "meritless." 993 F.3d at 139. The court confirmed that it "upheld [Kosinski's] conviction for insider trading" because "his explicit acceptance of a duty of confidentiality was itself sufficient to establish the fiduciary duty of trust and confidence that subjected his conduct to penalties for insider trading." *Id.* at 138 (quotation marks omitted). And the court described this case as the capstone in a line of circuit decisions imposing fiduciary-like status on "individuals who enter into such confidentiality agreements." *Id.* (citing, *e.g.*, *Falcone*, 257 F.3d at 234-35; *Chestman*, 947 F.2d at 567). *Chow* conclusively demonstrates that it is the government—not petitioner—that "misreads" the Second Circuit's decision.

The government also erroneously claims the petition rests on "factbound contention[s]" about this case. BIO.11. In fact, the petition challenges the Second Circuit's *legal* interpretation of this Court's precedents and its holding that, *as a matter of law*, a simple agreement to keep information confidential creates a duty to abstain from trading.

Moreover, this case is an ideal vehicle in which to resolve this question. The Second Circuit's prior decisions concerning confidentiality agreements all involved *breached* confidences—where individuals violated duties of confidentiality by "tipping" confidential information to others. *Falcone* involved an employee's unauthorized tips about confidential information from his employer, 257 F.3d at 227-28, and *Chestman* involved a husband's tip about confidential information he learned from his wife, 947 F.2d at 555. *Cf. United States v. Afriyie*, 929 F.3d 63, 68 (2d Cir. 2019) (contract specified duty of "confidence and trust"). But here the Second Circuit held that a contractual confidentiality obligation between arms-length counterparties not only prohibits disclosure but also creates an implied duty of trust that prohibits trading on the information oneself. By thus equating trust with confidence, the Second Circuit effectively excised trust from the "trust and confidence" requirement.

The Second Circuit's holding is impossible to square with this Court's insider-trading precedents. And, as the petition explains and *amicus curiae* further amplifies, if left undisturbed it will upend the nation's securities markets. The government does not contest either point.

II. This Court Should Review The Second Circuit's Standardless Approach To The Duty Element, Which Violates Due Process

The government also makes no attempt to defend the Second Circuit's description of the duty of trust and confidence as an amorphous and undefinable concept to be ascertained and applied case-by-case, *after* the fact. The court held that there is no single "appropriate standard" and no "exclusive test of fiduciary status, nor the proof necessary to sustain a conviction." Pet.App.24a, 29a.

The Second Circuit's "we know it when we see it" approach eschews any "ascertainable standard," violates due process, and has no place in the criminal law. *United States v. L. Cohen Grocery Co.*, 255 U.S. 81, 89 (1921); *see Johnson v. United States*, 576 U.S. 591, 595 (2015) (due process forbids "a criminal law so vague that it fails to give ordinary people fair notice of the conduct it punishes, or so standardless that it invites arbitrary enforcement"). And it is particularly problematic in the area of securities law, which "demands certainty and predictability" to guide market activities in advance. *Pinter v. Dahl*, 486 U.S. 622, 652 & 654 n.29 (1988). Criminal insider-trading liability cannot be imposed by after-the-fact judicial determinations that sweep in an ever-expanding range of previously non-fraudulent conduct. Rather, it is "essential…to have a guiding principle for those whose daily activities must be limited and instructed by…inside-trading rules." *Dirks*, 463 U.S. at 664.

The government does not contest any of this, and instead targets a straw man: It incorrectly presumes petitioner contends "[t]he concept of a relationship of 'trust and confidence'" is "unconstitutionally vague."

BIO.13; *see also* BIO.12 (suggesting petitioner claims "the securities laws, as interpreted in" prior Second Circuit precedents, are "void for vagueness"). But petitioner's due process arguments are not aimed at the securities laws, this Court's precedents, or the Second Circuit's earlier rulings. The question presented is whether "the Second Circuit's open-ended, case-by-case approach to the duty element" *adopted in this case* renders this Court's trust-and-confidence standard unconstitutionally vague. *Compare* Petition.i, *with* BIO.I (recasting second question as whether "the misappropriation theory" is unconstitutionally vague).

For this reason, the government's arguments against review are specious. Petitioner could not have forfeited his vagueness argument, *see* BIO.12, because what he challenges is the Second Circuit's pronouncement in this case that there is no ascertainable standard for identifying a duty of trust and confidence. Lacking a crystal ball, petitioner could not possibly have raised this argument *before* the Second Circuit issued its decision.

Likewise, it is entirely irrelevant that permissible "qualitative standards in criminal law" such as recklessness and willfulness exist, and that "[t]he concept of a relationship of 'trust and confidence' likewise lacks mathematical precision." BIO.13. The point is that to *avoid* such a problem, "trust and confidence" should be limited to situations where "[t]he existence of a fiduciary [or similar] relationship…[is] beyond dispute." *Skilling*, 561 U.S. at 407 n.41. Those are traditional relationships like the ones between corporate officers and shareholders (*Chiarella*, 445 U.S. at 227), employees and their employers (*Salman*, 137 S. Ct. 424), and lawyers and their clients (*O'Hagan*, 521 U.S. at 653). Without such limits, the open-ended approach taken by the Second Circuit here risks the "hopeless indeterminacy" that violates the Due Process Clause. *Sessions v. Dimaya*, 138 S. Ct. 1204, 1213 (2018).

The government also asserts that any vagueness problem is cured because the circumstances here "clearly constitute[] a relationship of trust and confidence." BIO.13. But as explained, the confidentiality provision did not establish the requisite fiduciary-like duty of trust. Nor did "the necessity of independence" and Kosinski's obligation to maintain "financial disconnection and objectivity" from Regado. BIO.8, 10. Quite the contrary: These factors normally counsel *against* a fiduciary relationship. *See* Petition.28. Accordingly, no statute, regulation, or court decision could have put Kosinski on notice that these circumstances might denote a fiduciary-like duty of "trust and confidence." The Second Circuit's mode of analysis—which applies the facts to the law, rather than the law to the facts—is hopelessly vague.[1]

Finally, the government argues that the Second Circuit merely applied its *Chestman* test, which

[1] Moreover, contrary to the government's suggestion, BIO.13, petitioner is entitled to argue that "trust and confidence" must be interpreted narrowly to avoid the vagueness problems inherent in the Second Circuit's approach. The canon of constitutional avoidance "is a tool for choosing between competing plausible interpretations of a statutory text," such that, "when a litigant invokes the canon of avoidance, he is not attempting to vindicate the constitutional rights of others…he seeks to vindicate his own *statutory* rights." *Clark v. Martinez*, 543 U.S. 371, 381-82 (2005).

identifies three specific qualities typically found in fiduciary relationships. BIO.12, 14. But that is not what the Second Circuit did. Instead, it held that "*Chestman*'s three-factor standard…does not state the exclusive test of fiduciary status," Pet.App.29a, and identified seven separate tests and an unbounded set of potentially relevant factors that can be used, after-the-fact, to justify a prosecutor's decision to label just about any relationship as one of "trust and confidence." In other words, under the Second Circuit's ruling, there is simply no ascertainable standard that marks the boundary between lawful and unlawful conduct. It fails to define the duty of "trust and confidence" "with sufficient definiteness that ordinary people can understand what conduct is prohibited, or in a manner that does not encourage arbitrary and discriminatory enforcement." *McDonnell v. United States*, 136 S. Ct. 2355, 2373 (2016) (quotation marks omitted). It is critical to the integrity of the securities markets and the liberty of investors and market professionals that this Court intervene to provide clarity in place of the Second Circuit's amorphous and dangerously standardless approach.

III. The Second Circuit's Approach To Harmless-Error Review Violates The Sixth Amendment And This Court's Precedents

The government apparently concedes that the district court incorrectly stated the law when it instructed the jury that a confidentiality agreement establishes a duty of trust and confidence. *See* BIO.15 (court "provide[d] the jury an incorrect definition of the term 'duty of trust and confidence'"); *id.* (instruction was "the error"). And the government does not deny that petitioner's conviction necessarily rests on legal error, because the erroneous instruction was the only path the jury was given to find the duty element.

Accordingly, the conviction cannot stand. An instructional error cannot be harmless unless the court finds "beyond a reasonable doubt that the error complained of did not contribute to the verdict obtained." *Neder*, 527 U.S. at 15. The Second Circuit never made, and could not have made, such a finding, because the only theory on which the jury was instructed was legally flawed. In other words, the error necessarily "contribute[d] to the verdict," so the conviction cannot stand. *Id.*; *see Grunewald v. United States*, 353 U.S. 391, 410-15 (1957) (if defendant convicted on "impermissible theory," court cannot affirm even if it "think[s] a jury could infer from th[e] evidence" facts sufficient to convict under permissible theory). But the Second Circuit refused to apply this settled law, which other circuits faithfully apply, and instead purported to make its own factual findings based on legal theories that were never submitted to the jury.

The government insists that the Second Circuit *did* determine "that the mistake did not contribute to the verdict," BIO.16, but those words appear nowhere in the court's decision. The Second Circuit turned a blind eye to what led to the actual verdict and instead speculated what "a rational jury would have found" had the government and the district court conducted the case differently. Pet.App.30a. Indeed, the Second Circuit could not possibly have concluded that the error did not contribute to the verdict, because the erroneous instruction told the jury that a confidentiality agreement, by itself, establishes the duty of trust and confidence.

For the same reason, the government's claim that the "duty of trust and confidence" element "*was* presented to the jury," BIO.15, is meritless. The government cites references to "trust and confidence" in its own summation, but this is a circular argument: Using the correct phrasing could not cure the problem because under the instruction, a confidentiality agreement by definition created a duty of "trust and confidence."

A conviction based on an erroneous instruction cannot stand if it is "possible" that the jury "convicted…for conduct that is not unlawful." *McDonnell*, 136 S. Ct. at 2375; s*ee Stromberg v. California*, 283 U.S. 359, 369-70 (1931) (conviction that may have rested "exclusively" upon an invalid theory "must be set aside"); *see also Chiarella*, 445 US at 237 n.21 ("We may not uphold a criminal conviction if it is impossible to ascertain whether the defendant has been punished for noncriminal conduct."). Here it was not just "possible"; it was indisputable. Because petitioner "contested the…[duty] element and raised evidence sufficient to support a contrary finding," the Second Circuit could "not find the error harmless." *Neder*, 527 U.S. at 19.

IV. This Court's Intervention Is Imperative To Curb The Second Circuit's Efforts To Rewrite Insider-Trading Law

Criminal laws—and the securities laws in particular—demand clarity, certainty, and judicial restraint. Yet in this case and several other recent rulings, the Second Circuit has steadily expanded the boundaries of insider-trading fraud, inviting prosecutors to pursue conduct that lies beyond the narrow bounds established by this Court. For example, in a tipping scenario "the test" of whether an insider has breached his duty "is whether the insider personally will benefit, directly or indirectly, from his disclosure." *Dirks*, 463 U.S. at 662; *accord Salman*, 137 S. Ct. at 427. Yet the Second Circuit has dispensed with this critical requirement, holding that it is sufficient that the insider intended to benefit the *tippee*. *United States v. Martoma*, 894 F.3d 64, 74 (2d Cir. 2017), *cert. denied*, 139 S. Ct. 2665 (2019). And the Second Circuit has attempted to eliminate the personal-benefit requirement entirely as to certain statutes with text virtually identical to the provisions construed in *Dirks* and *Salman*. *See United States v. Blaszczak*, 947 F.3d 19, 34-37 (2d Cir. 2019), *vacated on other grounds sub nom. Olan v. United States*, 141 S. Ct. 1040 (2021).

The Second Circuit's rulings in this area have nationwide impact given its outsized influence on securities law and the fact that virtually every securities transaction in some way touches Manhattan. Left unchecked, its decisions here and in other recent insider-trading cases present a serious threat to individual liberty and the stability of the securities markets.

It is time for this Court to intervene.

CONCLUSION

The Court should grant the petition.

Respectfully submitted,

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