SULLIVAN & CROMWELL LLP

October 1, 2020

DOJ and SEC Continue Insider Trading Enforcement

DOJ and SEC Bring Insider Trading Charges Against Index Manager

SUMMARY

On September 21, 2020, the United States Attorney for the Eastern District of New York announced the unsealing of a criminal complaint charging Yinghang "James" Yang with insider trading on the basis of confidential information misappropriated from his employer.[1] Yang and a co-conspirator were also named in a civil complaint filed by the Securities and Exchange Commission for the same alleged conduct.[2]

Yang is a senior index manager at a company whose operations include publishing several well-known stock market indices (the "Company").[3] At the Company, Yang is alleged to have served on an "Index Committee," which would occasionally meet to review potential changes to companies that make up certain U.S.-based indices.[4] The Company implements procedures to maintain the confidentiality of the Index Committee process, including by limiting the number of persons able to access Index Committee documents and information, given that changes to the indices are material, nonpublic information.[5] Over the course of several months in 2019, Yang and his purported friend and co-conspirator, Yuanbiao Chen, allegedly executed transactions relating to 14 issuers that were either added to, or removed from, stock market indices published by the Company.[6] Yang and Chen are accused of engaging in these transactions based on nonpublic information that Yang obtained through his employment.[7]

According to the complaints, the transactions generally followed the same pattern. First, either Yang or Chen, acting on information received from Yang, would purchase call or put options of an issuer hours ahead of a public announcement that the issuer would be added to, or removed from, one of the Company's indices.[8] Following that announcement, Yang and Chen would liquidate their positions for a profit.[9]

The transactions were allegedly executed through Chen's brokerage account, which was opened approximately one month after Chen received a $3,000 check from Yang.[10] The SEC alleged this enabled Yang to conceal the trading from his employer, which monitored Yang's personal brokerage account.[11] Chen purportedly misrepresented both his options-trading experience and his reasons for opening the account during the account-opening process.[12] Yang and Chen are alleged to have stopped such trading activity in October 2019, following a request from Chen's brokerage firm to fill out a form confirming Chen's occupation and sources of wealth.[13] In total, the trades that were made based on allegedly nonpublic information are purported to have resulted in more than $900,000 in illicit profits.[14]

The DOJ's criminal complaint charges Yang with conspiracy to commit securities fraud.[15] The SEC's civil complaint alleges two causes of action: (i) violations of Section 10(b) of the Securities Exchange Act of 1934, as amended, and Rule 10b-5, thereunder, against Yang and Chen,[16] and (ii) aiding and abetting violations of Section 10(b) and Rule 10b-5 against Chen.[17]

BACKGROUND

The U.S. Supreme Court has held that Section 10(b) prohibits individuals who owe a duty of trust and confidence from trading on material, nonpublic information in breach of that duty.[18] Under this misappropriation theory, such individuals also may not "tip" such inside information to others for the purposes of trading.[19] A tipper breaches his fiduciary duty when he discloses material, nonpublic information for a "personal benefit." A tippee who receives and trades on such information can also be liable for insider trading if "the tippee knows or should know that there has been a breach [of the insider's fiduciary duty]."[20]

The agencies alleged that Yang owed a duty of trust and confidence to the Company based on, among other things, the actions the Company took to protect the confidentiality of Index Committee discussions, the procedures and controls that the Company implemented to safeguard the Index Committee Process, and the Company's code of business ethics.[21]

IMPLICATIONS

These criminal and civil actions illustrate the continued emphasis of the DOJ and the SEC in bringing actions involving allegedly improper and fraudulent usage of material, nonpublic information. In particular, the cases are indicative of a unique risk of insider trading liability for employees who misappropriate confidential information from employers with potential influence over the markets. As the Director of the SEC's New York Regional Office, Richard R. Best, emphasized, "Financial professionals and other employees entrusted with confidential, market-moving information are prohibited from using that information for personal gain,"[22] even if they are employed to oversee indices. Seth D. DuCharme, Acting U.S. Attorney for the Eastern District of New York, echoed those sentiments, stating that Yang's arrest demonstrates that the DOJ is "committed to protecting the integrity of our financial markets from dishonest profiteers," and added that "Yang abused the trust placed in him by his employer and allegedly broke the law by trading on, and profiting from, non[-]public information that he stole from his employer."[23]

The agencies do not allege any misconduct or violation of law by the Company. Rather, the agencies focus on the policies and procedures that the Company implemented around the Index Committee process. Employers with potential market-moving information may wish to review their policies and procedures with respect to the confidentiality of that information, as well as their training programs.

* * *

ENDNOTES

1 *See Queens Man Charged in Insider Trading Scheme,* DOJ Press Release (Sept. 21, 2020), *available at* https://www.justice.gov/usao-edny/pr/queens-man-charged-insider-trading-scheme.

2 *See SEC Charges Index Manager and Friend with Insider Trading*, SEC Press Release 2020-217 (Sept. 21, 2020), *available at* https://www.sec.gov/news/press-release/2020-217.

3 SEC Compl. ¶ 14. It is widely reported that Yang is a Senior Index Manager at S&P Dow Jones Indices. *See, e.g*., Maria Armental, *Two N.Y. Men Accused of Trading on Inside Information From S&P Dow Jones Indices*, WSJ (Sept. 22, 2020).

4 SEC Compl. ¶¶ 38-39.

5 *See* SEC Compl. ¶ 40.

6 DOJ Compl. ¶¶ 30, 38, 40; SEC Compl. ¶ 46.

7 DOJ Compl. ¶ 30; SEC Compl. ¶ 46.

8 DOJ Compl. ¶ 39; SEC Compl. ¶ 46.

9 DOJ Compl. ¶ 39; SEC Compl. ¶ 46.

10 DOJ Compl. ¶¶ 32-33.

11 SEC Compl. ¶ 63.

12 SEC Compl. ¶¶ 43-44.

13 SEC Compl. ¶ 77; *see also* DOJ Compl. ¶¶ 48-50.

14 DOJ Compl. ¶ 44; SEC Compl. ¶ 2.

15 DOJ Compl. at 1.

16 SEC Compl. ¶¶ 78-80.

17 SEC Compl. ¶¶ 81-84.

18 *See* 15 U.S.C. § 78j(b); *United States* v. *O'Hagan*, 521 U.S. 642, 650-52 (1997).

19 *Dirks* v. *SEC*, 463 U.S. 646, 663 (1983).

20 *Id.* at 660.

21 SEC Compl. ¶¶ 40-42.

22 *Supra* n.2.

23 *Supra* n.1.

ABOUT SULLIVAN & CROMWELL LLP

Sullivan & Cromwell LLP is a global law firm that advises on major domestic and cross-border M&A, finance, corporate and real estate transactions, significant litigation and corporate investigations, and complex restructuring, regulatory, tax and estate planning matters. Founded in 1879, Sullivan & Cromwell LLP has more than 875 lawyers on four continents, with four offices in the United States, including its headquarters in New York, four offices in Europe, two in Australia and three in Asia.

CONTACTING SULLIVAN & CROMWELL LLP

This publication is provided by Sullivan & Cromwell LLP as a service to clients and colleagues. The information contained in this publication should not be construed as legal advice. Questions regarding the matters discussed in this publication may be directed to any of our lawyers listed below, or to any other Sullivan & Cromwell LLP lawyer with whom you have consulted in the past on similar matters. If you have not received this publication directly from us, you may obtain a copy of any past or future publications by sending an e-mail to SCPublications@sullcrom.com.

CONTACTS

New York

Nicolas Bourtin	+1-212-558-3920	bourtinn@sullcrom.com
David H. Braff	+1-212-558-4705	braffd@sullcrom.com
Robert E. Buckholz	+1-212-558-3876	buckholzr@sullcrom.com
Jacob M. Croke	+1-212-558-4895	crokej@sullcrom.com
Justin DeCamp	+1-212-558-1688	decampj@sullcrom.com
Robert W. Downes	+1-212-558-4312	downesr@sullcrom.com
Theodore Edelman	+1-212-558-3436	edelmant@sullcrom.com
Stephen Ehrenberg	+1-212-558-3269	ehrenbergs@sullcrom.com
Nicole Friedlander	+1-212-558-4332	friedlandern@sullcrom.com
Robert J. Giuffra Jr.	+1-212-558-3121	giuffrar@sullcrom.com
Richard H. Klapper	+1-212-558-3555	klapperr@sullcrom.com
Sharon Cohen Levin	+1-212-558-4334	levinsc@sullcrom.com
Ryne V. Miller	+1-212-558-3268	millerry@sullcrom.com
Sharon L. Nelles	+1-212-558-4976	nelless@sullcrom.com
Ann-Elizabeth Ostrager	+1-212-558-7357	ostragerae@sullcrom.com
Robert W. Reeder III	+1-212-558-3755	reederr@sullcrom.com
Frederick Wertheim	+1-212-558-4974	wertheimf@sullcrom.com
Stephanie G. Wheeler	+1-212-558-7384	wheelers@sullcrom.com
Samuel W. Seymour	+1-212-558-3156	seymours@sullcrom.com

Washington, D.C.			
	Judson O. Littleton	+1-202-956-7085	littletonj@sullcrom.com
	Kathleen S. McArthur	+1-202-956-7591	mcarthurk@sullcrom.com
	Aisling O'Shea	+1-202-956-7595	osheaa@sullcrom.com
	Christopher Michael Viapiano	+1-202-956-6985	viapianoc@sullcrom.com
	Kamil R. Shields	+1-202-956-7040	shieldska@sullcrom.com
Los Angeles			
	Adam S. Paris	+1-310-712-6663	parisa@sullcrom.com
	Robert A. Sacks	+1-310-712-6640	sacksr@sullcrom.com
	Anthony J. Lewis	+1-310-712-6615	lewisan@sullcrom.com
Palo Alto			
	Brendan P. Cullen	+1-650-461-5650	cullenb@sullcrom.com
	Laura Kabler Oswell	+1-650-461-5679	oswelll@sullcrom.com
London			
	Theodore Edelman	+44 20 7959 8450	edelmant@sullcrom.com