SEC Continues To Struggle In Insider Trading Jury Trials

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Brian E. Casey
Partner

By Brian E. Casey | The SEC's difficulties trying insider trading cases continued to mount this past week. Two different juries, in Texas and Illinois, concluded that the SEC failed to prove its allegations of insider trading in separate cases brought by the agency. These results form part of what seem to be a growing trend of losses in insider trading jury trials which perhaps may cause Chair Mary Jo White to temper the agency's enthusiasm for pushing the envelope in deciding what cases to try. They may also encourage defendants to press on to trial, knowing that the SEC's recent track record includes an increasing number of defeats. For the second time in a month, juries in the Northern District of Illinois rejected the SEC's insider trading theories in cases before them. On Jan. 27, a Chicago jury concluded that Rex C. Steffes and his three sons, Cliff, Bret, and Rex R. Steffes, were not liable for insider trading in connection with their purchases of shares of Florida East Coast Industries, Inc. (FECI) shortly before the company announced it was being acquired by Fortress Investment Group, LLC in May 2007. (Earlier in January, a jury concluded in less than an hour that Simang Yang had not committed insider trading in connection with his acquisition of options and stock of a Chinese company in advance of a corporate takeover.) In *SEC v. Steffes*, the agency alleged that Cliff Steffes learned of FECI's impending acquisition through his employment with a freight railway that FECI owned. Steffes allegedly tipped other members of his family, and they collectively purchased stock and options in FECI which ultimately resulted in over $1 million in profits to various family members once the acquisition was announced. However, the jury was unconvinced and found in favor of defendants after only about a day of deliberation. Then, on Feb. 3, a jury in the Western District of Texas handed down a verdict that was, in large part, another defeat for the SEC. In *SEC v. Life Partners Holdings, Inc.*, the jury cleared all the individual defendants of insider trading, and eight of the twelve claims asserted overall by the SEC. This case relates to the company's sale of life settlements, sometimes called viaticals, which the SEC has insisted for years fall within the definition of securities. In this case, the SEC alleged several different claims. First, it alleged that Life Partners, and several of its senior officers, including its CEO, CFO, and General Counsel, engaged in improper revenue recognition and also failed to disclose that its sale of life settlements was based on inaccurate and too brief life expectancy models. Second, the SEC alleged that its CEO (Pardo) and its CFO (Peden) engaged in insider trading and sold approximately $11.5 million and $300,000 of Life Partners common stock while failing to disclose the company's allegedly inflated financial condition. In a somewhat mixed verdict, the jury concluded that the corporate officers were not liable for insider trading, as well as the most serious allegations of accounting fraud. However, the jury

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did find that the company, and Pardo, were liable on four counts related to books and records violations, public certifications, and the company's revenue recognition policy. Following the adverse decisions in several recent insider trading cases (*Cuban*, *Schvacho*, and *Yang*), the SEC's continued difficulty in getting a jury to adopt its insider trading theories could present a challenge for one of the agency's oft-stated highest priorities –vigorously enforcing its prohibition on insider trading.