STILL COOKIN' IN DALLAS—FIFTH CIRCUIT REVERSES DISMISSAL OF INSIDER TRADING CHARGES AGAINST MARK CUBAN

September 27, 2010

To Our Clients and Friends:

As we predicted in our August client update, "What's Cookin' In Dallas? Court Dismisses Insider Trading Charges Against Mark Cuban," the SEC appealed the district court's dismissal of insider trading charges against Mark Cuban ("MC") relating to MC's sale of shares of Mamma.com Inc. (the "Company"). On September 21, 2010, the United States Court of Appeals for the Fifth Circuit (the "Court") vacated the district court's dismissal. The Court's decision is noteworthy due to the fact that it vacated the trial court's opinion on relatively narrow procedural grounds and declined to address the key substantive legal issue on appeal (*i.e.*, whether a duty of confidentiality, without more, is sufficient to support "misappropriation theory" insider trading liability).

Reading the complaint in the light most favorable to the SEC, the Court concluded that the allegations, taken in their entirety and assumed to be true for purposes of a motion to dismiss, provide at least a plausible basis to find that the Company's CEO and MC had reached a no-trade agreement with respect to MC's shares of the Company. The relevant allegations can be summarized as follows:

- In the spring of 2004, the Company's CEO told MC about a proposed PIPEs offering to gauge MC's interest in participating. He prefaced the conversation with disclosure regarding the confidential nature of the information he intended to share with MC. MC agreed to keep the information he received confidential.
- At the end of the conversation, MC expressed his displeasure regarding PIPEs generally and expressed the view that he was now precluded from selling by stating, "[w]ell, now I'm screwed. I can't sell." MC then asked to see the terms and conditions of the offering.
- The Company's CEO sent MC a follow-up e-mail giving MC the contact information for the placement agent, and MC called the agent and obtained additional information about the offering, including the fact that the offering was being sold at a discount to the market price.

- Following the call, MC sold all of his shares and avoided losses in excess of $750,000 by selling prior to the announcement of the PIPEs offering.
- MC did not inform the Company of his intention to trade on the information that he had been given in confidence and that he had agreed to keep confidential.

The SEC's claims against MC were based on the misappropriation theory of insider trading liability recognized by the Supreme Court in *United States v. O'Hagan*. Put simply, the theory holds that when a person other than a corporate insider misappropriates confidential information for securities trading purposes, in breach of a duty owed to the source of the information, that person violates the antifraud provisions of the federal securities laws. The key substantive question before the Court was whether the district court had erred in finding that a duty of confidentiality (in this case MC's agreement to maintain as confidential the fact of the PIPEs offering), without more, is insufficient to provide the requisite duty to support misappropriation theory liability. The Court by-passed the legal issue at the heart of that question and, instead, concluded that since the SEC's complaint had alleged that MC obtained access to the PIPEs pricing information only after expressing his view that he was precluded from selling, a plausible basis existed to conclude that the CEO and MC did, in fact, share an understanding that he was not to trade on the basis of his knowledge of the pending PIPEs offering. As such, the Court found that the SEC had sufficiently pled that MC owed a duty to the CEO to use the information solely for purposes of evaluating whether he would participate in the PIPEs offering and not for his personal gain (in this case, avoidance of loss).

The Court also declined to consider the lower court's conclusion that the SEC could not rely on Rule 10b5-2(b)(1) to provide the requisite duty for misappropriation theory liability. Rule 10b5-2 provides 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, and Rule 10b5-2(b)(1) provides that a duty of trust or confidence exists whenever a person agrees to maintain information in confidence. The lower court had determined that, since nothing in Rule 10b5-2(b)(1) requires that the confidentiality agreement encompass an obligation not to trade on or otherwise use the information, the SEC could not rely on it to establish MC's liability under the misappropriation theory.

* * * *

Given the profile of this prosecution and the fact that the key substantive issues presented by the district court's decision remain unresolved, and the importance of those issues to the SEC's enforcement program, we expect this case to continue to play out in the courts and will continue to report on relevant developments.

Please do not hesitate to call us to discuss the Court's decision in this matter or any of the issues raised by this memorandum generally.

Paul R. Berger
+1 202 383 8090
prberger@debevoise.com

Matthew E. Kaplan
+1 212 909 7334
mekaplan@debevoise.com

Jonathan R. Tuttle
+1 202 383 8124
jrtuttle@debevoise.com