June 1, 2021

Day Pitney White Collar Roundup - June 2021 Edition

Access Denied: Government's Interpretation of the CFAA Shut Down

In a 6-3 decision cutting across ideological lines, the U.S. Supreme Court recently considered the scope of the Computer Fraud and Abuse Act of 1986 (CFAA) in *Van Buren v. United States*. In the case, Nathan Van Buren, a former police sergeant, ran a license plate number through a law enforcement database in return for a cash payment. Van Buren had authority to access the database, but no authority to use it for a non-law enforcement purpose. He was charged with violating the CFAA, which imposes criminal liability on anyone who "intentionally accesses a computer without authorization or exceeds authorized access" and thereby obtains computer information. 18 U.S.C. § 1030(a)(2). The statute defines "exceeds authorized access" to mean "to access a computer with authorization and to use such access to obtain or alter information in the computer that the accesser is not entitled so to obtain or alter." § 1030(e)(6). Penalties under the CFAA range from fines and misdemeanors to imprisonment, and the statute also provides for a private cause of action.

Under the government's theory, Van Buren, by knowingly violating his department's computer search policy, also violated the CFAA by using a computer network "contrary to what [his] job or policy prohibits." Under this approach, the circumstances under which a person's conduct would be illegal could be derived from a broad range of sources—U.S. Code, state statute, private agreement, policy or otherwise. As a result, the approach could criminalize a wide range of activities, from major violations to the more mundane, such as employees who shop online using a work computer when company policy prohibits them from doing so. The *Van Buren* majority, however, decided that an individual exceeds authorized use only when they obtain information to which their computer access did not extend, rather than when they misuse information they are otherwise entitled to access. Because of this, the CFAA protects against gaining unauthorized access to a computer or, if granted access, from obtaining information located in files, folders, databases or other areas that are off-limits to them. But it does not encompass individuals who, like Van Buren, have "improper motives for obtaining information that is otherwise available to them."

In addition to tightening up the scope of criminal liability, the *Van Buren* decision may also shift the balance of power from companies, firms and other employers—which may have relied on the CFAA to discourage employees from misusing access to company information—to employees, who now may argue that they need to show only that they had authority to access the information in question, regardless of motivation or misuse. As such, companies would do well to review their computer use policies in order to clarify exactly what information is accessible and to whom. Otherwise, access may be anything but denied.

SEC Seeks Stop to Stock Trading Shenanigans

If you are an executive of a publicly traded company, you probably have a Rule 10b5-1 trading plan (or you should consider one). Rule 10b5-1 allows a corporate insider to establish a formal trading plan that specifies prescheduled dates or criteria for selling the insider's stock. This kind of trading plan can be invaluable in fighting off securities fraud claims alleging the insider took advantage of material nonpublic information to dump stock before a negative corporate disclosure. In essence, Rule

10b5-1 allows an insider who trades in company shares to rebut the inference of scienter (i.e., intentional wrongdoing) by showing the trades were scheduled *before* the insider learned of a coming negative disclosure.

But in remarks issued in early June, SEC Chair Gary Gensler announced that "these plans have led to real cracks in our insider trading regime," and he has tasked his staff with making "recommendations for the Commission's consideration on how we might freshen up Rule 10b5-1." He identified four key areas of concern:

- When insiders or companies adopt 10b5-1 plans, there is no cooling-off period required before they make their first trade. This means insiders could attempt to strategically insulate themselves by adopting plans within days or weeks of a significant corporate event. A cooling-off period of four to six months could help minimize that risk.
- There are no limitations on when 10b5-1 plans can be canceled. This creates risk that an executive, with the benefit of having new insider information, will rush to cancel an order to sell under an existing plan.
- There are no mandatory disclosure requirements regarding 10b5?1 plans, including around when they are adopted or modified. Greater transparency may promote confidence in the market.
- There are no limits on the number of 10b5-1 plans that insiders can adopt. This creates risk that an insider might adopt multiple plans then decide to keep the favorable plan and cancel the troubling ones.

Gensler is not the first to identify the potential for abuse and opportunism under the existing Rule 10b5-1. His recent remarks noted bipartisan support for the need to update the rule, including from his immediate predecessor, former SEC chair Jay Clayton. The SEC has not revealed a timeline for its potential refresh. Of course, we need not wait on the SEC. For some time, companies committed to best practices have been setting limitations on 10b5-1 plans to reduce many of the risks Gensler highlighted. Now may be a good time for others to consider a proactive "refresh" of their own plan rules.

SCOTUS Declines Review of Insider Trading Conviction

The U.S. Supreme Court recently denied a Connecticut physician's request to review his conviction for insider trading. The case highlights that the rules forbidding insider trading may apply not only to traditional corporate insiders but also to anyone in a fiduciary relationship or the functional equivalent with a publicly traded corporation.

According to the opinion of the U.S. Court of Appeals for the Second Circuit, Dr. Edward Kosinski was a principal investigator for Regado Biosciences Inc. in connection with the company's clinical trial of a drug designed to stop blood clotting in patients undergoing heart procedures. During the course of the clinical trial, Kosinski bought $250,000 of the company's stock without disclosing the position, in breach of an agreement with the trial administrator to disclose his holdings in the company if they exceeded $50,000. Later, Kosinski was informed that the clinical trial would be suspended due to safety concerns after patients exhibited allergic reactions. The following morning, and before that information was made public, Kosinski sold off all his Regado Biosciences shares, ultimately allowing him to avoid a loss of approximately $160,000.

In November 2017, Kosinski was convicted of two counts of securities fraud-insider trading in violation of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5. He was sentenced to six months of imprisonment, two years' supervised release and a $500,000 fine.

On appeal, the Second Circuit considered whether Kosinski owed a fiduciary duty to Regado Biosciences to not trade its stock using confidential, nonpublic information. The court answered in the affirmative for two primary reasons. First, the court concluded that Kosinski, as a principal investigator for the clinical trial, was a "temporary insider" similar to accountants or lawyers who receive corporate information through their work and thereby enter into a "special confidential relationship" with the corporation. Second, the court found that Kosinski's relationship with Regado Biosciences was "fiduciary in nature because it was a relationship based upon trust and confidence," including because he had agreed to keep the company's

information confidential and to disclose his holdings if they exceeded a threshold that could affect his assessment of the drug. For those reasons, among others, the court affirmed the insider trading conviction.

Kosinski petitioned the Supreme Court to take another look, arguing that the Second Circuit was wrong in determining, in essence, that a confidentiality agreement suffices to establish a fiduciary or similar relationship of trust and confidence for purposes of the statutes proscribing insider trading. Mark Cuban, entrepreneur and owner of the Dallas Mavericks, also threw his support behind Kosinski, asking the Court to review the case and arguing that the Second Circuit improperly imposed liability for insider trading absent Kosinski undertaking any duty of trust or loyalty to the company.

With the Supreme Court's denial of Kosinski's petition, the Second Circuit's decision remains applicable law – law that serves as a reminder that the prohibitions on insider trading may now apply well beyond traditional corporate insiders.

Cosby Saga Continues With Unexpected Reversal

The reversal of Bill Cosby's rape conviction by the Pennsylvania Supreme Court at the end of June has elicited an array of passionate responses, most of which focus on issues of justice and equity in sexual assault matters. But the decision is actually not about sexual assault and, instead, was decided on narrow procedural grounds.

Cosby had been investigated by State District Attorney Bruce Castor. Castor issued a press release in 2016 announcing he was closing the investigation, asserted he had found that a conviction would be "unattainable" and encouraged the parties to resolve the issue in a civil suit. Castor said in the press release, and in later proceedings, that he believed it would assist the victim in a civil case if he spoke as the "sovereign" and removed the possibility of prosecution, thus, in his view, eliminating Cosby's ability to invoke the Fifth Amendment in civil proceedings.

Apart from the press release, there was no formal immunity agreement, no plea agreement and no formal proceedings under Pennsylvania's statute that prescribes the process for granting immunity (a process that requires the participation of a judge). Cosby was in fact sued civilly and was deposed. Apparently relying on the viewpoint outlined by Castor, he did not invoke the Fifth Amendment and answered a number of questions, under oath, regarding the underlying events involving the victim and other women.

Castor was replaced as district attorney by Risa Ferman, who reopened the investigation and charged and ultimately convicted Cosby of rape. The evidence included the incriminatory statements made by Cosby at the civil deposition.

The decision by the Pennsylvania Supreme Court focuses on the Fifth Amendment issue and finds that Cosby had, in essence, been promised immunity and relied on that promise in testifying at the civil deposition, and that the subsequent district attorney was bound by that promise. Cosby's conviction was reversed, and he was released from prison the same day.

What might this mean for litigators? For criminal practitioners, it underscores the complexity of negotiating with prosecutors, even where there are apparent clear statutory lines. Plea bargaining and even pre-charge discussions involve elements of contract and equity that may later result in unintended consequences. In the Cosby case, it worked out well for the defendant, although it is not at all clear this was due to clever foresight by defense counsel. For civil litigators, the case illustrates how complicated the intersection between criminal and civil law can be, particularly in the area of Fifth Amendment rights.

New Jersey's Own to Lead Enforcement Division

New Jersey Attorney General Gurbir S. Grewal recently announced that he is stepping down from his role as the state's chief law enforcement officer to lead the SEC's Enforcement Division. Grewal starts his new role on July 26 and will serve under SEC Chair Gary Gensler. His appointment comes after the abrupt resignation of the former director of enforcement, Alex Oh, who served in that role for six days.

Since assuming office as the 61st (and first Sikh American) attorney general of New Jersey in January 2018, Grewal oversaw legal issues for the state, including civil and regulatory matters, as well as all state, county and local law enforcement officers and prosecutors. He gained notice for participating in numerous lawsuits against the administration of former President Trump and for being active in the areas of police reform and gun control. Prior to serving as attorney general, Grewal served as the Bergen County prosecutor and led the Economic Crimes Unit at the U.S. Attorney's Office for the District of New Jersey. Gensler, pointing to Grewal's distinguished career in law enforcement, expressed confidence that Grewal "has the ideal combination of experience, values, and leadership ability to helm the Enforcement Division at this critical time." It's no small order, but Grewal appears poised for the challenge.

Authors

Helen Harris

Partner

Stamford, CT | (203) 977-7418

hharris@daypitney.com

Mark Salah Morgan

Partner

Parsippany, NJ | (973) 966-8067

New York, NY | (212) 297-2421

mmorgan@daypitney.com

Stanley A. Twardy, Jr.

Of Counsel

Stamford, CT | (203) 977-7368

satwardy@daypitney.com