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M&A Attorneys: Little They Can Do to Curb Insider Trading

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Word last month of a settlement between the U.S. Securities and Exchange Commission and a former executive of GSI Commerce over charges the executive encouraged insider trading in advance of GSI's sale to eBay was an example of dozens of insider trading cases the SEC brings every year.

And for the mergers and acquisitions attorneys working on public company deals, the policing of insider trading is something that has to fall largely on the shoulders of the SEC and the public companies themselves.

"It depends on the company and what sort of in-house staff they have," said Gary A. Miller, chairman of Eckert Seamans Cherin & Mellott's securities and corporate finance practice. "I would think that for a larger company that has significant in-house staff, the M&A lawyer probably leaves it to them to deal with people on issues outside of the deal itself."

But for the smaller companies he represents, Miller said he would tend to ensure that, once the deal gets to a certain point, the executives know not to trade until something is publicly announced. A number of companies, he said, will send out notices to all employees informing them of a blackout period for trading without disclosing exactly why the company wants to put a stop to trading for a certain timeframe.

Mergers and acquisitions lawyers may keep an eye on the public trading data that is easily available, Miller said. But it is usually difficult to catch an individual engaged in insider trading that way.

"The SEC tracks that," Miller said. "I don't think most lawyers have the capacity."

While Saul Ewing's mergers and acquisitions group co-chairman, David S. Antzis, said he doesn't know that a lawyer has a duty to monitor a client's trading activity during deal discussions, the lawyer could advise corporate leadership to educate employees on trading policies. But beyond that, there isn't much an M&A lawyer can do.

"It's hard for me to believe that, in today's world, high-level executives don't know that they should not be trading your stock," Antzis said. "It doesn't really matter what memoranda you distribute. ... You can't stop something that is done by somebody that doesn't have the best of intentions."

Antzis said he may notice if a client's stock is trading at 10 times the volume of a normal day, but trading isn't something he monitors every day when in the midst of a deal. He said that is the SEC's role.

"It shouldn't be a lawyer's job to monitor whether a client's doing illegal things," Antzis said. "It's just making sure the clients know it's illegal, and in the case of public company executives, they know [insider trading is] illegal."

But still, Antzis said he is surprised at the amount of deals that are later found to have involved insider trading.

According to the latest available SEC statistics, there were 44 insider-trading enforcement actions in 2013, down from 58 in 2012 and 57 in 2011. The peak over the last 10 years was in 2008, when there were 61 actions filed, according to the SEC statistics.

In the case of the eBay-GSI deal, Christopher Saridakis, the former head of GSI's marketing solutions division, was alleged by the SEC to have told two family members and two friends of the impending deal and encouraging them to trade on that information, according to a statement from the SEC. Those four then told others about the information. Some of the "tippees" cooperated with the SEC. As part of his settlement with the SEC, Saridakis agreed to never serve as an officer or director again and to pay \$664,822, which includes a penalty equal to twice the amount of his tippees' profits, the SEC said.

"Although Saridakis' tips spun a web of illegal trading, some of the downstream tippees substantially assisted in our investigation while others hindered it," said Andrew J. Ceresney, director of the SEC's Division of Enforcement, in a statement. "The reduction in penalties for those tippees who assisted us, together with the nonprosecution agreement for one of the traders, demonstrate the benefits of cooperating with our investigations. The increased penalties for others highlight the risks of impeding our work."

Drinker Biddle & Reath corporate and securities lawyer Doug Raymond said he views his role as one of not just ensuring his clients don't break the laws on insider trading that many executives are already aware of, but also making sure they don't do anything that could cause the SEC to open an investigation regardless of whether charges are ultimately filed.

"The people who are involved in transactions like this are very sophisticated and they do know basically what's going on, but I also think that it is incredibly important to remind them ... you're not necessarily trying to help them win the lawsuit when it's filed ... you are trying to avoid ever getting that call in the first instance," Raymond said. "So it just requires being more sensitive to these issues than just staying on the right side of the law."

That might mean not just advising against trading their own stock, but as was the issue in the GSI matter, advising them not to have any family or friends trade the stock or even mention the deal they are working on to a family or friend who may on their own determine to make a trade based on that information, Raymond said.

The actions a lawyer could take in curbing any potential insider trading could vary depending on the situation. Antzis said there could be a difference between whether the lawyer is representing the target company or the acquiring company.

"If you are representing the target company, at some point, everybody who is part of the company is liable to do trading and it's almost impossible for you to be able, as a lawyer, to advise everybody in the company 'you are in the process of being bought, so don't trade the stock,'" Antzis said.

He said his firm has a memorandum it gives to clients that could be sent to all of the employees advising them that there may be rumors a deal is in the works and that they should not trade the stock.

As a buyer, only a few people in the company typically know in the beginning that a deal is in the works, Antzis said. At that point, an M&A lawyer could easily tell those few people to avoid selling the stock.

"You might assume the senior executives know better, but it might not hurt," Antzis said.

Raymond said companies will often have policies that encourage senior executives to be long-term investors of the company rather than someone who buys and sells stocks frequently. But if frequent trading is necessary for estate planning purposes, for example, Raymond said executives may want to look into a safe-harbor program that sets up frequent trades based on a certain calculus—such as selling 100 shares every week or only buying when a stock hits a certain price. Raymond said the SEC won't question trades under such a plan even if they happen during an M&A deal.

Where lawyers do have a significant duty, Antzis said, is in making sure they themselves keep information confidential. Investment bankers who have lawyers as friends, for example, may just make a friendly call to see what deals lawyers are working on, Antzis said. In that case, the lawyers have to keep the information to themselves.

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