New Trend Admitting Wiretap Evidence in Insider Trading Cases

Until recently, the use of wiretap evidence was limited to the prosecution of crimes that are specifically enumerated in Title III of the Omnibus Crime Control and Safe Streets Act of 1968, codified at 18 U.S.C. 2510-2522. Such evidence has typically been admitted primarily in drug cartel, alien smuggling and organized crime cases, but until now it has not been used in securities fraud cases. The times have changed. In the last several months, federal courts have twice upheld the use of wiretap evidence in insider trading prosecutions. Defendants Raj Rajaratnam and other ex-Galleon Group traders were found guilty of securities fraud by juries that listened spellbound to damning evidence from wiretapped telephone calls. Although the use of wiretap evidence is still generally prohibited in insider trading and other cases not enumerated in Title III, these recent rulings suggest that the reliance on wiretap evidence may be allowed in *any* case in which the wiretap was authorized in the investigation of an enumerated crime, even if that crime is not itself prosecuted.

Wiretaps and Congressional Goals

Congress' intent in passing Title III was to strike a balance between allowing wiretapping as an investigative tool and safeguarding the privacy of the general public and investigative targets. Wiretapping is one of the most invasive tools in law enforcement's arsenal, and Title III reflects a strong Congressional desire to circumscribe its use. *See, e.g., Berger v. New York*, 388 U.S. 41, 63 (1967) ("Few threats to liberty exist which are greater than that posed by the use of eavesdropping devices."); *Gelbard v. United States*, 408 U.S. 41, 48 (1972) (*quoting* S. Rep. No. 1097, 90th Cong., 2d Sess., 66 (1968)); U.S. Code Cong. & Admin. News, p. 2153 ("To assure the privacy of oral and wire communications, [T]itle III prohibits all wiretapping and electronic surveillance by persons other than duly authorized law enforcement officers engaged in the investigation or prevention of *specified types* of serious crimes, and only after authorization of a court order obtained after a showing and finding of probable cause.") (emphasis added). Accordingly, Title III enumerates the only types of predicate offenses upon which law enforcement may rely in seeking authorization for a wiretap.

Title III requires government agents monitoring calls via wiretap to avoid listening to, or to "minimize" the interception of, calls that are not authorized for interception. *See* 18 U.S.C. § 2518(5). Title III also provides a suppression remedy for those unlawfully subjected to the interception of their wire or oral communications, but courts avoid applying the remedy harshly, *see* 18 U.S.C. § 2515 and *Scott v. United States*, 436 U.S. 128 (1978), instead employing a generous reasonableness analysis when determining whether or not to suppress wiretap evidence.

Expansion of Wiretap Use to Insider Trading Prosecutions

Securities fraud (insider trading) is not among the enumerated offenses. Nonetheless, in *United States v. Rajaratnam*, 2010 WL 4867402, *1 (S.D.N.Y. Nov. 24, 2010), Judge Richard Holwell held that evidence obtained from wiretaps was admissible at trial. He reasoned that because wire fraud is an authorized crime under Title III, and because the government used wiretaps to investigate a fraudulent insider trading scheme using interstate wires, the wiretap evidence was admissible at trial. Judge Holwell carefully avoided ruling that wiretaps are generally permissible in insider trading cases. Rather, he held that evidence of securities fraud discovered through a wiretap based on an authorized crime under Title III (wire fraud, in this case) was permissible. If securities fraud is committed without the use of a wire, Title III will preclude the use of wiretapping. *Rajaratnam*, at *6 n.8.

Even though Judge Holwell attempted to circumscribe the potential reach of *Rajaratnam*, his opinion may prove to be the gateway to broader usage of wiretapping in white-collar and other cases. In fact, his ruling was followed in another securities fraud case, *U.S. v. Goffer*. The defendants advanced two arguments against the admission of wiretapped conversations. First, they argued that Title III prohibited the use of wiretaps because securities fraud is not an enumerated predicate offense. Second, they contended that the government had to comply with Title III's minimization requirement. Defendants' Reply Memorandum in Further Support of their Joint Motion to Dismiss and Suppress, *U.S. v. Goffer*, No. 10-CR-0056 (RJS), ECF 115 (Dec. 17, 2010). The government had intercepted

nearly 200 personal calls between one of the defendants, Craig Drimal, and his wife. Judge Richard Sullivan characterized the interception of martial communications as "disgraceful," "egregious," "an embarrassment generally," and "inexcusable and disturbing," especially because many intimate calls were monitored by agents long after they realized that the conversations did not relate to their investigation, with one six-minute call being monitored for at least four minutes. *Goffer*, Memorandum and Order, ECF 179 (Apr. 20, 2011).

Notwithstanding his distaste for the government's conduct, however, Judge Sullivan did not suppress any relevant intercepted calls, either on the grounds of illegality, or as a sanction for the government's misconduct. He summarily rejected the defendants' arguments that the wiretapping was illegal due to the lack of an authorized predicate offense. And, notwithstanding the government's voyeuristic intrusion into private calls, he found that, "on the whole, the wiretap was professionally conducted and generally well-executed." *Id.* The wiretap evidence was subsequently introduced at trial.

Civil, as Well as Criminal, Cases to Be Affected

This innovative use of wiretap evidence may begin to change the legal landscape in certain civil cases, as well. The Securities Exchange Commission brought a civil action against Rajaratnam, parallel to his criminal prosecution. It sought to obtain wiretap evidence from Rajaratnam and his co-defendant, Danielle Chiesi, obtained in the criminal case and disclosed to Rajaratnam and his co-defendants. District Judge Jed Rakoff, presiding over the S.E.C. action, ruled that the S.E.C. was entitled to its production. *S.E.C. v. Galleon Mgmt.*, LP, 683 F. Supp. 2d 316 (S.D.N.Y. 2010).

On appeal, the Second Circuit held that, "nothing in Title III bars the use of the fruits of authorized wiretaps obtained in the pursuit of investigations of suspected crimes that are listed in Title III in securities fraud or insider trading proceedings." *S.E.C. v. Rajaratnam*, 622 F.3d 159, 173 (2d Cir. 2010). On remand, Judge Rakoff held that whatever privacy interests the defendants had were outweighed by the S.E.C.'s right of access to the wiretap intercepts, and therefore ordered Rajaratnam and Chiesi to disclose it. *S.E.C. v. Galleon Mgmt.*, LP, 2011 WL 1770631 (S.D.N.Y. May 20, 2011).

In light of *Goffer*, *Rajaratnam*, and Fed. R. Evid. 403 as applied in the civil context, it seems likely that Judge Rakoff will permit the introduction of wiretap evidence.

The impact of his ruling may be felt even by those who are not the intended subjects of wiretaps. The *New York Times* has reported that the S.E.C. may file a federal enforcement proceeding against Rajat Gupta, the former managing director of McKinsey & Company and an alleged co-conspirator with Raj Rajaratnam. *See* Peter Henning, *Focus on Insider Trading Becomes More Intense*, DealBook (August 8, 2011, 3:50 pm), http://dealbook.nytimes.com/2011/08/08/focus-on-insider-trading-becomes-more-intense/. If it does so, it will almost certainly seek to admit wiretap evidence gleaned during the Rajaratnam investigation that allegedly reveals the nature of Gupta's involvement in insider trading. *Id.* Assuming the S.E.C. files suit and satisfies the requirements of the "co-conspirator exception" to the hearsay rule, Gupta could find himself in a difficult position in court, defending himself against statements made by Rajaratnam during a wiretapped telephone call to which he was not a party. *Id.*

Implications for the Future

Rajaratnam could be interpreted as rendering admissible in *any* criminal proceeding wiretap evidence collected in the investigation of an authorized crime under Title III. Federal prosecutors pursuing insider trading cases have certainly taken notice of U.S. Attorney Preet Bharara's success in prosecuting Wall Street insiders, and will seek to apply his innovative strategy. Bharara "took wiretaps for a test drive, and I'd say it was a resounding success," opined Stephen Miller, a former federal prosecutor. *See* Larry Neumeister & Tom Hays, *Wiretaps Key in Conviction of Ex-Hedge Fund Giant*, ABC News (May 12, 2011), http://abcnews.go.com/US/wireStory?id=13585543.

Judge Rakoff has already permitted wiretap evidence to be used in prosecuting an insider-trading case against James Fleishman of Primary Global Research, LLC. Memorandum, *United States v. Fleishman*, No. 11-CR-32 (JSR), ECF 115 (Aug. 31, 2011). Fleishman had argued that there was insufficient probable cause for the wiretaps, which targeted 104 Primary Global telephone line users, because there was no showing that all 104 individuals had engaged in wrongdoing. *See* Andrew Longstreth, *Expert-networking Defendant Challenges Wiretap*, Reuters (Aug. 2, 2011, 9:25 am), http://www.reuters.com/article/2011/08/02/us-fleishman-wiretapidUSTRE77103T20110802. However, Fleishman declined to challenge the wiretaps' validity on the grounds that insider trading is not an enumerated predicate offense under Title III.

Meanwhile, U.S. Attorney Bharara has made it clear his office will continue to prosecute insider trading cases based on wiretap evidence. When insider traders adopt "the methods of common criminals, such as the use of anonymous cell-phones, we have no choice but to treat them as such. To use tough tactics in these circumstances is not being heavy-handed; it is being even-handed," Bharara stated in remarks to the New York City Bar last year. *See* Bruce Carton, *SDNY's Bharara Focuses on Insider Trading, Wiretaps*, Compliance Week (Oct. 27, 2010) http://www.complianceweek.com/sdnys-bharara-focuses-on-insider-trading-wiretaps/article/191929/.

Insiders using non-public information should consider carefully a question Bharara has posed: "Today, tomorrow, next week, the week after, privileged Wall Street insiders who are considering breaking the law will have to ask themselves one important question: Is law enforcement listening?" United States Attorney Preet Bharara, Prepared Remarks for Press Announcement (October 16, 2009).