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Second Circuit Clarifies Scope of Insider Trading Liability

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Any time the Second Circuit issues a reasoned opinion on insider trading, the opinion bears notice. Last month the Second Circuit clarified the scope of insider trading liability in the context of information only derivatively related to a public company. In so doing, the court sidestepped an opportunity to resolve an intriguing trading issue (discussed below) that would have had far more compelling consequences.

In a 3-0 opinion, the Second Circuit cleared Goldman Sachs and Morgan Stanley of allegations that they traded while in possession of inside information. *In re Archegos 20A Litig.*, No. 24-1162, 2025 LX 394588 (2d Cir. Sep. 16, 2025). While the facts of the case are complicated and somewhat unusual, they can be summarized as follows.

Morgan Stanley and Goldman Sachs engaged in a series of securities transactions known as total return swaps or TRS contracts on behalf of a family office run by criminally-convicted Sung Kook ("Bill") Hwang, formerly of Tiger Asia Management, LLC. Pursuant to the TRS contracts, the two institutions purchased large positions in seven public companies including ViacomCBS and Discovery, Inc., which left the family office, Archegos Capital Management, L.P. (Archegos), with a beneficial interest in the stock of each company. To protect themselves, Morgan and Goldman purchased large amounts of the same companies for their own account.

Events combined over time to trigger a margin call by the banks which Archegos could not meet. Knowing Archegos's delicate financial position and aware that its failure could depress the share price of the seven stocks, the banks dumped their shares which triggered a downward spiral in the companies' stocks thereby damaging retail purchasers. Morgan and Goldman were sued in a series of class actions alleging trading while in possession of material nonpublic information.

The appeal was preceded by a decision by Judge Jed Rakoff to dismiss the consolidated complaint for failure to adequately allege a breach of fiduciary duty or similar relationship. After engaging in analyses under both the classical and misappropriation theories of insider trading, the Second Circuit affirmed. In doing so, the Court found that Archegos was not a corporate insider or otherwise owed a fiduciary or fiduciary-like duty to

the issuers' shareholders nor did the banks owe such a duty to Archegos. Its decision was based on the facts that Archegos – despite its large positions in the seven companies – was not a controlling shareholder or insider and Archegos and the banks negotiated at arm's length with Archegos (i.e., they did not assume fiduciary-like obligations).

While the opinion comported with generally accepted principles of insider trading, the Court specifically sidestepped a more intriguing question: whether possession of nonpublic information about the financial condition of a third-party and the likely impact of that information on a public company could qualify as inside information about the public company for section 10(b) purposes. The answer in this case turned on the lack of a fiduciary duty but the presence of such a duty could have affected the outcome significantly.

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