

SHADOW TRADING: THE FIRST TEST FOR THE SEC'S NOVEL THEORY

The first test of the Securities and Exchange Commission's ("SEC") shadow trading theory in federal court has resulted in a win for the agency. On January 14, 2022, a federal district court denied defendant Matthew Panuwat's motion to dismiss the SEC's complaint, permitting the case to go forward on a theory of "shadow trading."¹ Shadow trading is where corporate insiders exploit material nonpublic information ("MNPI") about their company, to trade in the securities of an "economically-linked" company, such as a similarly situated competitor. For an in-depth discussion of the case and the shadow trading theory, [see our prior client alerter](#).

In upholding the SEC's shadow trading allegations, U.S. District Judge William H. Orrick ruled that the SEC's complaint adequately alleged that Panuwat's conduct breached his duty to his company, Medivation Inc., when he traded in a competitor's shares after obtaining MNPI about Medivation's upcoming merger with Pfizer. While acknowledging that there "appear[ed] to be no other cases where the [MNPI] at issue involved a third party," the district court concluded that "the SEC's theory of liability falls within the general framework of insider trading, as well as the expansive language of Section 10(b) and corresponding regulations." It was "commonsense," in the district court's view, that MNPI may be material to more than two companies. The district judge also dismissed Panuwat's purported lack of notice, finding that "[t]he SEC has sufficiently alleged that Panuwat acted with scienter, and therefore had notice that his purported actions were prohibited by law."

Of particular interest to whether Panuwat breached a duty to Medivation in misappropriating MNPI is Medivation's corporate policy, which stated,

During the course of your employment...with the Company, you may receive important information that is not yet publicly disseminated...about the Company. ... Because of your access to this information, you may be in a position to profit financially by buying or selling or in some other way

¹ Order Denying Motion to Dismiss, *Securities and Exchange Commission v. Panuwat*, No. 21-cv-06322-WHO (N.D. Ca. Jan. 14, 2022).

dealing in the Company's securities...or the securities of another publicly traded company, including all significant collaborators, customers, partners, suppliers, or competitors of the Company. ... For anyone to use such information to gain personal benefit...is illegal. ...²

Although Panuwat did not trade in either Medivation or Pfizer securities, he did trade in securities of Incyte, a competitor likely to be affected by the Medivation-Pfizer merger, and thus plainly covered by Medivation's insider trading policy. Under the circumstances, it was difficult for Panuwat argue lack of notice and lack of breach of duty. Companies are well-advised to ensure that their insider trading policies similarly prohibit trading in any securities, even those of a third-party company or competitor, to avoid being caught in any "shadow trading" crosshairs.

² Complaint, *Securities and Exchange Commission v. Panuwat*, No. 21-cv-06322-WHO, ¶ 20 (N.D. Ca. Aug. 17, 2021).

CONTACTS

John Friel
Partner

T +1 212 878 3386
E john.friel
@cliffordchance.com

Robert Houck
Partner

T +1 212 878 3224
E robert.houck
@cliffordchance.com

Celeste Koeleveld
Partner

T +1 212 878 3051
E celeste.koeleveld
@cliffordchance.com

Daniel Silver
Partner

T +1 212 878 4919
E daniel.silver
@cliffordchance.com

Benjamin Berringer
Associate

T +1 212 878 3372
E benjamin.berringer
@cliffordchance.com

Alexandra Coyle
Associate

T +1 212 880 5719
E alexandra.coyle
@cliffordchance.com

E. Carlisle Overbey
Associate

T +1 212 878 8504
E carlisle.overbey
@cliffordchance.com

Benjamin Peacock
Associate

T +1 212 878 8051
E benjamin.peacock
@cliffordchance.com

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Clifford Chance, 31 West 52nd Street, New York, NY 10019-6131, USA

© Clifford Chance 2022

Clifford Chance US LLP

Abu Dhabi • Amsterdam • Barcelona • Beijing • Brussels • Bucharest • Casablanca • Delhi • Dubai • Düsseldorf • Frankfurt • Hong Kong • Istanbul • London • Luxembourg • Madrid • Milan • Moscow • Munich • Newcastle • New York • Paris • Perth • Prague • Rome • São Paulo • Shanghai • Singapore • Sydney • Tokyo • Warsaw • Washington, D.C.

Clifford Chance has a co-operation agreement with Abuhimed Alsheikh Alhagbani Law Firm in Riyadh.

Clifford Chance has a best friends relationship with Redcliffe Partners in Ukraine.