



On January 14, 2022, a federal district court in the Northern District of California [declined to dismiss](#) the first-ever enforcement action by the U.S. Securities and Exchange Commission (the "SEC") based on allegations of "shadow trading" — the use of one company's inside information to trade in securities of another, similarly situated, but unrelated company.

In a typical insider trading case brought under Section 10(b) of the Securities Exchange Act of 1934 ("Section 10(b)"), liability is limited to trading on the basis of material, non-public information specific to the company in which the trading at issue occurred. The court's decision in *SEC v. Panuwat*, therefore, may signal an expansion of insider trading enforcement.

The defendant, Matthew Panuwat, worked at Medivation, an oncology-focused biopharmaceutical company. When he joined Medivation, Panuwat signed the company's insider trading policy, which prohibited him from buying or selling Medivation's securities "or the securities of another publicly traded company, including all significant collaborators, customers, partners, suppliers, or competitors of" Medivation while in possession of "important" non-public information about Medivation. During the course of his employment, Panuwat learned that Medivation would be acquired by Pfizer. The SEC alleges that Panuwat purchased call options in a competing biopharmaceutical company, Incyte, within minutes of learning about the acquisition. When the merger was later announced, stock prices for Incyte and Medivation both rose. In August 2021, the SEC filed suit against Panuwat, alleging that his purchase of Incyte call options constituted insider trading in violation of Section 10(b).

In Panuwat's motion to dismiss the SEC's complaint, he argued that the SEC's shadow trading theory was an improper attempt to expand the scope of existing insider trading law to "punish innocent conduct without a valid legal basis or fair notice to market participants." The court disagreed, noting that the SEC's claims were premised on the existing "misappropriation theory" of insider trading. Under the misappropriation theory, a defendant is liable for insider trading under Section 10(b) if he or she knowingly misappropriates material, non-public information for securities trading purposes, in breach of a duty owed to the source of the information. Although the court acknowledged that the SEC's theory of liability in this case was "unique," it nevertheless held that the SEC had adequately pleaded each of the required elements under the misappropriation theory: materiality, breach of duty, and scienter.

- **Materiality:** Significantly, the court held that the SEC had sufficiently alleged that the Medivation acquisition would be material information to an Incyte investor. Given the limited number of mid-cap, oncology-focused biopharmaceutical companies, the acquisition of one of them (i.e., Medivation) might make other companies (i.e., Incyte) more attractive to investors, which could then drive up their stock price. Accordingly, the court noted that a reasonable investor would consider the acquisition important in deciding whether to buy or sell Incyte stock.
- **Breach of Duty:** The court also held that the SEC had adequately pleaded that under Medivation's insider trading policy, Panuwat owed the company a duty not to trade in the securities of any other "publicly traded company" when in possession of non-public information about Medivation. Therefore, the Court found that Panuwat's trading in Incyte was in breach of his duty under Medivation's policy.
- **Scienter:** Finally, the court found that the SEC had sufficiently alleged that Panuwat actually used the information about Medivation's acquisition when he purchased the Incyte stock. The court pointed to allegations that Panuwat had never traded in Incyte before and traded "within minutes" of learning about the impending acquisition.

While *Panuwat* may signal an effort by the SEC to expand insider trading liability, the impact of the court's decision may be limited. The court based its decision in part on the fact that Medivation's internal policy broadly prohibited trading in the securities of "another publicly traded company." In the absence of such language, it is unclear whether an individual would owe his employer a duty not to trade in the securities of another, unrelated company. Moreover, while the SEC's shadow trading theory may have survived Panuwat's motion to dismiss, it has yet to prevail at trial. Nevertheless, this decision should serve as a reminder to companies to review their insider trading policies and educate their employees accordingly.

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