



On November 20, 2023, a federal district court in the Northern District of California [declined to grant summary judgment to the defendant](#) in *SEC v. Panuwat*, the first-ever enforcement action by the U.S. Securities and Exchange Commission (the "SEC") based on the novel insider trading theory of "shadow trading"—the use of one company's inside information to trade in securities of another, similarly situated, but unrelated company.

The court previously [declined to dismiss](#) the case, [signaling a potential expansion of insider trading enforcement](#). The court's summary judgment decision provides further guidance as to what may constitute impermissible shadow trading ahead of a trial scheduled for March 2024.

The case centers on Pfizer's acquisition of Medivation, an oncology-focused biopharmaceutical company. The defendant, Matthew Panuwat, worked at Medivation and allegedly learned the acquisition was imminent when Medivation's CEO emailed Panuwat and other employees about the status of the sale process. Seven minutes later, Panuwat purchased call options in another oncology-focused biopharmaceutical company, Incyte, which he later sold for a profit. In its January 2022 decision denying Panuwat's motion to dismiss, the court held that the SEC had adequately pleaded each of the required elements under the well-established "misappropriation theory" of insider trading: materiality, breach of duty, and scienter. In its recent summary judgment decision, the court held that the SEC had shown genuine disputes of material fact concerning each of those elements and elaborated on materiality and breach of duty for purposes of the shadow trading theory.

As to materiality, the court held that the relevant inquiry for the shadow trading theory is whether there is a "market connection" between the company from which the inside information came (Medivation) and the company that issued the traded security (Incyte). The court rejected Panuwat's contention that the SEC's theory of liability would too broadly reach "some or all other allegedly similar biopharmaceutical companies" in the same sector as Medivation. Instead, the court focused on the connection between the two companies "as part of a niche section of the biopharmaceutical market" in a "small pool" of companies "where scarcity was at least speculated to translate into market value." The court ruled that there was a market connection between Medivation and Incyte even though the two companies were not direct competitors. In so ruling, the court relied on analyst reports and news articles stating that the Medivation acquisition could affect Incyte's prospects.

As to breach of duty, the court addressed two new theories of liability regarding Panuwat's alleged breach. At the motion to dismiss stage, the court held that the SEC had adequately pleaded that Panuwat breached a duty he owed to Medivation under the company's insider trading policy. At summary judgment, the court further ruled that the SEC had made a sufficient factual showing based on: (i) Panuwat's breach of Medivation's Confidentiality Agreement, which prohibited Panuwat from using the company's confidential information for his own personal benefit; and (ii) Panuwat's breach of a duty of trust and confidence, which arose under agency law when Medivation entrusted Panuwat with confidential information. The court ruled that there was a genuine dispute of material fact regarding whether Panuwat breached the latter duty by trading on the confidential information for his own personal benefit without disclosure to Medivation.

The court's summary judgment decision in *Panuwat* sends conflicting messages about the breadth of insider trading liability under the SEC's shadow trading theory. Several aspects of the decision indicate that the shadow trading theory can only apply to a narrow set of factual circumstances. For example, under the "market connection" test for materiality, the court expressly rejected the broad premise that a market connection would exist between two companies in the same industrial sector that are "allegedly similar." Instead, the court emphasized the scarcity of companies in Medivation and Incyte's niche section of the biopharmaceutical market. On the other hand, other aspects of the court's decision indicate that the shadow trading theory can apply to a broader set of circumstances. For example, the court found the materiality element satisfied even though Medivation and Incyte were not direct competitors. And the court's acceptance of two additional grounds for breach of duty that were absent from the motion to dismiss decision means that the shadow trading theory is not limited to companies with far-reaching insider trading policies like Medivation's. Trial is scheduled to begin on March 25, 2024, and companies and traders would be well-advised to follow along—how a jury reacts to the SEC's case should help crystallize any further shadow trading lessons.

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