

## CLIENT ALERT

### New SEC Case a Reminder that Hedge Fund Internal Analyses Can Constitute "Inside Information"

Oct.08.2014

On September 30, 2014, the Securities and Exchange Commission (SEC) brought charges against two individuals in a case that reflects the SEC's expansive view of insider trading and poses a cautionary tale to investment managers.

#### Brief Summary

The SEC's orders allege that Filip Szymik and Jordan Peixoto engaged in insider trading in Herbalife securities in advance of Pershing Square Management, L.P. (Pershing) releasing a presentation regarding its negative view of Herbalife on December 20, 2012. Szymik was the friend and roommate of a Pershing financial analyst, who told Szymik about the presentation in advance of the release and in violation of Pershing's written compliance policies. The financial analyst cautioned Szymik that the information was highly confidential and should not be traded upon.

Szymik nevertheless tipped his friend Peixoto, who purchased eight out-of-the-money Herbalife put options shortly before the presentation was released. A day after the release, the value of Peixoto's put options jumped to \$339,421. Apparently fearing the appearance of insider trading, Peixoto requested that his brokerage firms permit some of his profitable options to expire. One broker refused, and Peixoto ultimately obtained \$47,100 in actual profits.

#### Takeaways

This case reflects the misappropriation theory of insider trading, an expansive view of insider trading that focuses on information obtained through a breach of a relationship of trust and confidence. Here, even though Szymik was unaffiliated with Pershing, the charge against him is premised on a theory that he breached a duty of trust to his friend and roommate to keep information confidential while cognizant that Peixoto could trade on it. The financial analyst, who actually violated Pershing compliance policies, only seems to have escaped being charged on the basis that he warned Szymik not to tell anyone.

As to investment managers, these charges serve as a reminder that "insider information" does not have to involve leaks of earnings and other corporate announcements, but can include a manager's analyses and evaluations that could materially impact a stock's price. As such, it is imperative to have clear policies in place regarding the protection of such information. A manager without such a policy very well could have faced an enforcement action for ineffective compliance as a result of the analyst's breach of confidence.

Investment managers should exercise considerable caution to ensure that they maintain and enforce proper compliance programs. Such programs can not only provide guidance in a sometimes murky area of the law but also distance managers from potential misconduct.

The SEC's orders can be found [here](#) and [here](#).

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

**Daniel L. Zelenko**

Partner – New York

Phone: +1 212.895.4266

Email: [dzelenko@crowell.com](mailto:dzelenko@crowell.com)

**Thomas A. Hanusik**

Partner – Washington, D.C.

Phone: +1 202.624.2530

Email: [thanusik@crowell.com](mailto:thanusik@crowell.com)