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THE SEC'S SCRUTINY OF INSIDER TRADING IN AN ERA OF ALTERNATIVE DATA

In September 2021, the SEC, for the first time, brought charges of insider trading against a provider of alternative data that sold such data to trading firms but was not itself trading using that data. The upshot was a 10 million dollar civil penalty for the company, and a penalty and three-year bar for the former CEO. In this article, the authors discuss the case in detail, characterizing it as "a sea change" in the boundaries of the securities laws with respect to the sale and use of alternative data. They close with steps data providers and their customers should consider in light of the SEC's scrutiny.

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Alternative data, which is commonly defined as investment research from non-traditional means such as web traffic, app usage, or mobile device data, is increasingly used by investment firms and fund managers to provide advice to clients. Regulators are also scrutinizing the use of alternative data. The Securities and Exchange Commission's Division of Enforcement filed the first-ever enforcement action in 2021 against an alternative data provider, and the SEC's Division of Examinations¹ ("Exams") has identified the use of alternative data in investment advising and trading as an examination priority. The SEC's focus is whether the alternative data that trading firms are receiving includes material non-public information ("MNPI") (as some alternative data is derived from non-public sources), privacy issues (as some of the data includes consumers personal data), and relatedly, the integrity of the market where trading firms are able to acquire this non-traditional form of information that is unavailable to retail investors.

¹ The SEC's Division of Examinations was previously the Office of Compliance Inspections and Examinations.

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In September 2021, the SEC brought charges against a provider of alternative data that sold data to trading firms, but itself was not trading using that data, representing a sea change in the boundaries of the securities laws with respect to the sale and use of alternative data. With the SEC's expressed priorities and areas of focus, and in light of this novel enforcement action, alternative data will be an ongoing area of scrutiny for the agency. This article will discuss what alternative data is, how it is being used by investment firms to provide advice, review the SEC's renewed focus on this issue over the last year, review a recent and novel SEC enforcement action related to the use of alternative data, and provide several key considerations for data providers and investment firms that are considering the use of alternative data in providing investment advice.

WHAT IS ALTERNATIVE DATA?

Alternative data is an amorphous category of information that investors can rely on to inform their investment decisions. Alternative data encompasses many different types of information, including location

INSIDE THIS ISSUE

● **TRADING FOREIGN COMMODITY FUTURES AND OPTIONS BY U.S. PERSONS, Page 7**