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SEC V. MARK CUBAN — COULD THIS CASE REPRESENT A SEA CHANGE?

By Steven Siesser, Esq., Matthew Oliver, Esq., and Bernard Cooney, Esq.

May 28, 2009

A federal judge in Dallas heard arguments Tuesday in the high-profile insider trading case brought by the United States Securities and Exchange Commission against Mark Cuban, the well-known and outspoken owner of the Dallas Mavericks. The SEC sued Cuban, alleging that he unlawfully used material, non-public information to sell stock that he knew was about to decline in value, and thus avoided losses of \$750,000. This case could have profound implications for the manner in which capital market participants handle material, non-public information, especially around capital raising transactions.

In this case, the SEC alleges that Cuban, the largest shareholder of a public company called Mamma.com, was informed by the company's CEO of an impending capital raise through a private investment in public equity (PIPE). In a brief

telephone conversation, the CEO asked Cuban if he would agree to keep the information the CEO was prepared to convey to him confidential. Cuban agreed and, in reliance on his promise to maintain confidentiality, the company informed Cuban that it was planning a PIPE and asked if he was interested in participating. Rather than expressing interest, Cuban became very upset and informed the CEO that the PIPE would dilute existing shareholders. According to the SEC, Cuban expressed frustration that, as a result of having come into possession of material, non-public information, he would not be able to sell any stock until the company publicly announced the offering. The following day Cuban promptly sold all his shares in the company. The company later announced the PIPE and the price of its shares dropped. As a result of his sale, Cuban allegedly avoided losses of \$750,000.

Yesterday's argument involved Cuban's motion to dismiss the SEC's

complaint. Cuban's chief argument is that he did not violate the legal prohibitions against insider trading merely by breaching an oral confidentiality agreement. The securities laws, Cuban argues, require that the trader violate a fiduciary or similar duty of trust and confidence owed to the issuer. Even if the allegations of the Complaint were true and a confidentiality agreement was established by virtue of the brief telephone call, Cuban argues that no court has ever held that a confidentiality agreement alone creates a fiduciary duty to act loyally to the source of the information. Violations of agreements may give rise to a civil cause of action for breach of contract, but do not without more rise to the level of a breach of duty sufficient to create insider trading liability.

Resolution of this case may have a significant impact on the manner in which investment banking clients and

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their issuer clients present PIPE and other opportunities to potential investors, particularly with respect to the procedures under which they bring investors "over the wall." Typically, the company or the investment bank identify potential investors and then, prior to sharing any information, obtain the investor's oral agreement to treat the information about to be conveyed as confidential and not to be used for securities trading purposes. This is a

well-established industry practice. This oral agreement to maintain confidentiality also satisfies the issuer's obligations under Regulation FD, which, incidentally, belies Mr. Cuban's position. However, if Cuban prevails and persuades the Court that an oral agreement is insufficient to establish the requisite relationship of trust and confidence, investment banks and issuers may need to substantially revise their existing procedures. For example, bankers

may be required to obtain written acknowledgements of a fiduciary relationship from the potential investor rather than just relying on oral assurances.

We will continue to monitor the developments in this case, and publish further updates as they are warranted.

In the interim, please feel free to contact your attorneys in the firm's [Specialty Finance Group](#) or otherwise at the firm with any questions.

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Boston

One Bowdoin Square
Boston, MA 02114
617 725 0036

New York

1251 Avenue of the Americas
New York, NY 10020
212 262 6700

Palo Alto

590 Forest Avenue
Palo Alto, CA 94301
650 433 5800

Roseland

65 Livingston Avenue
Roseland, NJ 07068
973 597 2500

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