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Rule 10b5-1 Amendments: Guidance for Issuers, Insiders, and Financial Intermediaries

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Agenda

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Background

Rule 10b5-1

- Rule 10b5-1 specifies that a sale constitutes trading on the basis of material non-public information (MNPI) when the person making the sale was aware of MNPI at the time the sale was made
- Rule 10b5-1, adopted in August 2000, codifies the position of the Securities and Exchange Commission (SEC) that awareness, not use, of MNPI is sufficient to establish liability in insider trading cases
- The rule creates a mechanism whereby any person or entity can enter into a trading plan that will provide an affirmative defense to a claim that a trade occurred “on the basis of” MNPI

Rule 10b5-1 *(cont'd)*

Available to persons and entities: Provides that trades made pursuant to trading plans established in compliance with Rule 10b5-1 are deemed not to have been made on the basis of MNPI

Available to entities: Provides that an entity will not be liable if it demonstrates the person making an investment decision on behalf of the entity was not aware of MNPI and that the entity had implemented reasonable policies and procedures to prevent insider trading

- *An issuer may also rely on 10b5-1 for itself.* An issuer should indicate that it is not in possession of MNPI when, for example, it enters into a stock repurchase program, an accelerated share repurchase program, etc.
- A **Rule 10b5-1 plan** is a trading program designed to comply with Rule 10b5-1(c) of the Securities Exchange Act of 1934, as amended (Exchange Act)

Elements of a Rule 10b5-1 Plan

- To benefit from the protections of the affirmative defense, a 10b5-1 plan must:
 - Specify the amount, price, and date of the purchases or sales;
 - Include a written formula for determining the amount, price, and date of the purchases or sales; or
 - Not permit the person to exercise any subsequent influence over how, when, or whether to effect the purchases or sales

Concerns Behind the Amendments

- Courts and legislators expressed concern that plan liability protections enabled insiders to opportunistically trade based on MNPI while technically complying with the Rule. Academic studies confirmed validity of concerns. Examples include:
 - Insiders trading under plans consistently outperform trading by other insiders not trading under plans
 - Insiders making trades soon after adopting or modifying a plan are disproportionately large
 - Insiders using multiple overlapping plans to selectively cancel certain trades using MNPI
 - Insiders timing gifts of securities while aware of MNPI
 - Issuers using plans to make share repurchases to boost share price ahead of insider sales
 - Issuers granting stock options to insiders in coordination with release of MNPI
- Rules address such concerns through a combination of plan regulation and disclosure requirements



Cooling-Off Periods

Cooling-Off Periods

- Does not apply to issuers
- For directors and executive officers (as defined by Rule 16a-1(f))
 - Trades may not begin until the later of:
 - 90 days, and
 - 2 business days after filing of Form 10-K or Form 10-Q for the quarter during which the plan was adopted (not to exceed 120 days)
 - Practical difficulties relying on SEC filings for 10b5-1 plans
- For all other persons (e.g., employees, large stockholders) cooling-off period of 30 days
- Modification constitutes termination of plan; requires starting a new cooling-off period



D&O Certifications

D&O Certifications

- Directors and executive officers required to make certification in plan that:
 - individual is not aware of any MNPI, and
 - plan is being adopted in good faith and not part of a plan or scheme to evade the prohibitions of the rule



No Overlapping Plans

No Overlapping Plans

- Does not apply to issuers, but to all others seeking to rely upon the affirmative defense of the rule
- May not enter into a new plan while having another Rule 10b5-1 plan outstanding (with 3 exceptions):
 - 1) Separate plans with different brokers that together constitute a single plan permitted
 - 2) “back-to-back” plans are permitted if transactions under the second plan do not begin until transactions under the first plan are completed or expire (new cooling-off period required if earlier plan terminated)
 - 3) “sell-to-cover” plans to satisfy tax withholding only upon vesting are not considered outstanding or additional plans (e.g., vesting of RSUs)



Single-Trade Plans Limited

Single-Trade Plans Limited

- Does not apply to issuers, but to all others seeking to rely upon the affirmative defense of the rule
- If not an eligible “sell-to-cover” plan and is designed to effect purchase or sale of all securities in a single transaction
 - then, individual may not have entered into another Rule 10b5-1 plan similarly designed during the prior 12-month period



Acting in Good Faith

Acting in Good Faith

- To have the benefit of the affirmative defense, person must enter into plan in good faith (existing requirement)
- Must now also act in good faith with respect to the plan
- New requirement intended to deter manipulation of timing of issuer disclosures by those in a position to do so



New Public Company Disclosure Requirements

New Disclosure for Public Companies

- Quarterly disclosure of adoption or termination of 10b5-1 plans and “non-Rule 10b5-1 trading arrangements” by officers and directors (but not the issuer)
 - Applies to public companies using domestic forms (*e.g.*, Form 10-Q and Form 10-K) (*i.e.*, not applicable to foreign private issuers (FPIs))
 - Disclosures would be required to include the name of the insider and the material terms (other than price) of the 10b5-1 plan or arrangement, such as:
 - Date of adoption or termination;
 - Duration; and
 - Number of securities to be sold or purchased; and
 - Whether intended to satisfy Rule 10b5-1

New Disclosure for Public Companies

- Annual disclosure of internal insider trading policies and procedures designed to promote compliance by directors, officers and the issuer, with insider trading laws
 - If an issuer has not adopted such policies it would have to disclose why it has not done so
 - Insider trading policies themselves must be included as an exhibit
 - FPIs to make similar annual disclosures in Form 20-F
- Unlike the proposal, issuers are not required to describe their policies and procedures within the body of the periodic report. Instead, insiders must disclose the existence of insider trading policy and file it as an exhibit
- Posting to the website is not enough

New Disclosure for Public Companies

- New Executive Compensation Disclosure: Option Grants and Similar Equity Instruments Made Close in Time to the Release of MNPI
 - Required in Form 10-K and certain proxy and information statements
 - No exemption for SRCs or EGCs; but not required for FPIs
 - Narrative disclosure of policies/practices regarding the timing of awards and release of MNPI, including
 - how the board determines when to grant awards;
 - whether (and how) the board takes MNPI into account when determining the timing and terms of an award; and
 - whether the company has timed the release of MNPI for purposes of affecting the value of executive compensation

New Disclosure for Public Companies

- Tabular disclosure of awards, on an award-by-award basis, granted to NEOs/directors in the period beginning (i) four business days before the filing of a periodic report (10-Q or 10-K), or current report on Form 8-K that contains MNPI (other than an 8-K disclosing the grant); and (ii) ending one business day after filing such report:
 - Date of grant, number of securities granted, exercise price and fair value at grant date
 - Percentage change in closing price of underlying stock between the trading days prior to and following disclosure

Name	Grant date	Number of securities underlying the award	Exercise price of the award (\$/Sh)	Grant date fair value of the award	Percentage change in the closing market price of the securities underlying the award between the trading day ending immediately prior to the disclosure of material nonpublic information and the trading day beginning immediately following the disclosure of material nonpublic information
PFO					
PFO					
A					
B					
C					



Section 16 Reporting Requirements

Gift Reporting

- *Bona fide* gifts to be reported on Form 4 within 2 business days
 - Previously, could be reported on Form 5 due 45 days after fiscal year-end (or voluntarily earlier on a Form 4)
 - Late filings must be disclosed in proxy statement
- Gifts of securities are subject to insider trading laws
 - Amendments designed to curb potential abuses through gifts
- Rule 10b5-1 is available for gifts
 - But new reporting schedule applies whether or not the gift is considered part of a Rule 10b5-1 plan

Amendment to Form 4s and 5

- Amendments add a mandatory Rule 10b5-1 checkbox to Forms 4 and 5
- Accompanying text indicates that reported transaction is intended to satisfy the affirmative defense conditions of Rule 10b5-1(c)
 - Check this box to indicate a transaction was made pursuant to a contract, instruction or written plan intended to satisfy the affirmative defense conditions of Rule 10b5-1(c)
- Confirm the EDGAR platform being used for Section 16 filings is adding the checkbox
- Companies that have been identifying Rule 10b5-1 trades in Form 4 footnotes may want to consider whether to continue this practice
- SEC did not adopt the proposed optional checkbox for non-Rule 10b5-1 plans



Inline XBRL

XBRL Tagging Requirements

- Inline XBRL tagging required for:
 - Item 402(x) of Regulation S-K
 - policies and practices related to the grant of certain equity awards close in time to the release of MNPI
 - Item 408(a) of Regulation S-K
 - Adoption or termination of a 10b5-1 plan by any director or officer
 - Item 408(b)(1) of Regulation S-K
 - Disclosure of whether issuer has insider trading insider trading policies and procedures
 - Item 16J(a) of Form 20-F
 - Insider trading policies



Effective Dates and Transition Issues

Effective Dates and Transition Periods

- **Rule 10b5-1 amendments will be effective February 27, 2023**
 - No phase-in for compliance with the new Rule 10b5-1 requirements
 - Rule 10b5-1 amendments do not impact existing 10b5-1 plans, *unless modified*
- Disclosure and Inline XBRL tagging requirements become effective beginning with filings covering the first full fiscal period beginning on or after April 1, 2023
- Smaller reporting companies have an additional six-months for transition, with compliance required covering the first full fiscal period beginning on or after October 1, 2023
- Section 16 reporting persons must comply with the amendments to Forms 4 and Forms 5 filed on or after April 1, 2023



Considerations for Issuers

Informing Persons Impacted by the Amendments

- Make directors, officers, and other employees aware of new Rule 10b5-1 requirements
 - Cooling-off periods, modifications, and restrictions on overlapping and single-trade plans
- Inform compensation committees of new disclosures for certain equity compensation awards
- Inform directors and officers of Form 4/two-business-day reporting of gifts
- Explain insider trading policies and procedures to covered persons

New Disclosure Controls and Procedures

- As a priority, update Rule 10b5-1 trading practices
 - Ensure there is a procedure for directors and officers to notify the company when they adopt or terminate a 10b5-1 plan
 - Require copies of new or modified 10b5-1 plans and confirm compliance with new requirements
- Also collect information regarding non-10b5-1 plans
- Be sure to add a disclosure control for exhibit filing requirement

Equity Award Considerations

- Consider a disclosure control to track when certain equity awards are made close in time to MNPI
 - Monitor grants within four business days before and one business day after filings of periodic or current reports
- Compensation committees should consider whether to revise grant schedules
 - Consider impact of narrative and tabular disclosure if awards if timing raises appearance of taking advantage of MNPI timing

Issuer Policies

- Update insider trading policies to reflect Rule 10b5-1 and disclosure amendments
- Consider adopting formal insider trading policies to avoid negative disclosure
- Consider how to address use of 10b5-1 plans
 - Encourage use of 10b5-1 plans
 - Require of 10b5-1 plans
 - No position on use of 10b5-1 plans other than compliance with rule
- Consider whether insider trading policy should be updated with respect to:
 - Pre-clearance
 - Blackout/window periods
 - Gifts

Issuer Share Repurchases

- Issuers are not subject to cooling-off periods or restrictions on multiple, overlapping trading plans and single-trade plans
- Issuers repurchasing shares under Rule 10b5-1 must act in good faith
- SEC remains concerned about issuer use of 10b5-1 plans
 - SEC is considering need to mitigate risk of issuer misuse of 10b5-1 plans
- Latest SEC regulatory agenda targets April 2023 for final share repurchase disclosure rule
 - Public companies should monitor the SEC's share repurchase rulemaking

Additional Considerations

- Greater focus on insider trading and MNPI
- Additional disclosures could lead to additional scrutiny
 - Potential for increased enforcement and litigation
 - Prepare investor relations to respond to questions in this area
- Consider administrative impact
 - Are there sufficient employees to handle new disclosure controls?
 - Any training needed?



Concerns for Investment Banks

Concerns for Investment Banks

- Investment banks will want to review their forms of 10b5-1 trading plans
- Plans for issuers:
 - Many issuers rely on Rule 10b5-1 in connection with repurchase plans and with other transactions
 - Investment banks will want to review the representations and warranties related to Rule 10b5-1 contained in their various forms
- The forms related to issuer repurchases will need to be reviewed and revised again once the SEC adopts final amendments to the rules related to share repurchase disclosures

Concerns for Investment Banks *(cont'd)*

- Plans for directors, officers, insiders and employees: these forms will need to be revised to ensure that the appropriate cooling off periods are addressed; additional representations are added regarding compliance with the issuer's policy, adoption in good faith, no entry while in possession of MNPI, no other plans in place; etc.
- Brokers may want to diligence any other permissible plans that are in place and may want copies or representations regarding these
- The broker may want a covenant regardless reporting and disclosure
- In conjunction with amending these plans brokers may want to address Form 144 filing and have the individual make the filing given electronic filing requirements

Additional Resources

Read more:

- [SEC Adopts Amendments to Rule 10b5-1's Affirmative Defense to Insider Trading Liability & Related Disclosures](#)
- [MB Microtalk Video: Rule 10b5-1 and Share Repurchase Disclosure Clawback Listing Standards Requirement: US SEC Adopts Final Rules](#)
- [SEC Proposes Amendments to Rule 10b5-1's Affirmative Defense to Insider Trading Liability](#)
- [Establishing an Issuer Rule 10b5-1 Plan with an ATM Offering](#)
- [What's the Deal? – 10b5-1 Plans](#)
- [FWP Blog: New Data Tagging Requirements for Annual Reports Filed in 2022](#)



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