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ALERTS

SEC Adopts Amendments To Rule 10b5-1 Trading Plans

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Highlights

New SEC rule amendments limit the use of multiple Rule 10b5-1 plans and add a cooling-off period prior to use

The new rule amendments require the individual adopting the plan to certify they are acting in good faith

Issuers must now disclose Rule 10b5-1 policies annually and use of such plans quarterly

On Dec. 14, 2022, the U.S. Securities and Exchange Commission (the SEC) adopted amendments to Rule 10b5-1 under the Securities Exchange Act of 1934, as amended, which, among other things, provides corporate insiders (i.e., officers and directors of an issuer) with an affirmative defense to insider trading liability if they trade securities pursuant to a written securities trading plan executed when the insider was not aware of material nonpublic information.

The amendments respond to growing concern among regulators and others that the plans were prone to abuse and that investors lacked necessary information about their use. The new amendments, thus, do two main things: 1) add new conditions to the availability of the Rule

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10b5-1(c)(1) affirmative defense, and 2) enhance insider and issuer disclosure obligations related to the adoption and use of Rule 10b5-1 plans.

Subject to certain transition periods, these amendments will become effective 60 days after publication of the adopting release in the Federal Register. Issuers and corporate insiders should consider reviewing their plans and policies to ensure that they comply with these changes by early next year.

The amendments to Rule 10b5-1 now require corporate insiders to:

- Abide by a “cooling-off” period after adopting a new or modified Rule 10b5-1 trading plan before engaging in any trading pursuant to the plan; and
- Make two important certifications at the time of the adoption of the new or modified Rule 10b5-1 plan providing that the insider (i) is not aware of any material nonpublic information about the issuer or its securities, and (ii) is adopting the plan in good faith and not as part of a plan or scheme to evade the prohibitions of Rule 10b-5.

With respect to the new cooling-off requirements, Rule 10b5-1(c)(1) now requires a cooling-off period before any trading can commence under a Rule 10b5-1 trading plan, for director and officers of the issuer of the later of 1) 90 days following plan adoption or modification, or 2) two business days following the disclosure in certain periodic reports of the issuer’s financial results for the fiscal quarter in which the plan was adopted or modified (but not to exceed 120 days following plan adoption or modification). The amended rule also requires a cooling-off period of 30 days for persons other than issuers, or the officers and directors of issuers, before any trading can commence under a Rule 10b5-1 plan.

Under the amendments, corporate insiders are also limited to relying on this affirmative defense for a single-trade plan to one such plan per any consecutive 12-month period. Moreover, the amended rule now limits the ability of anyone other than issuers to use multiple overlapping Rule 10b5-1 plans. The amended rule further requires all persons entering into a Rule 10b5-1 plan to act in good faith with respect to the plan.

New Disclosure Requirements

With respect to the new disclosure requirements, the amended rule now requires issuers to disclose:

- Comprehensive information about the issuer’s policies and procedures related to insider trading, including making quarterly disclosures of the use of Rule 10b5-1 plans by and other trading arrangements with the company’s directors and officers; and
- Certain tabular and narrative disclosures regarding awards of options when made close in time to the release of material nonpublic information.

Filers of SEC Forms 4 and 5 (which respectively require certain insiders

to disclose changes in their holdings as they occur and annually) must also indicate by checking a box if a reported transaction was intended to satisfy the affirmative defense conditions of Rule 10b5-1(c).

The SEC asserts the amendments to Rule 10b5-1 add much needed clarity and structure for corporate insiders seeking to design a compliant and workable Rule 10b5-1 plan. The SEC also believes the amended rule will improve transparency for members of the investing public, who, according to the SEC, previously had a limited view of issuers' policies regarding trading pursuant to these plans.

As with any new or amended regulatory regime, time will tell whether these goals are accomplished. That being said, the rule amendments will have important implications for public companies, including requiring disclosure of what may be sensitive policies and procedures surrounding insider transactions and corporate governance practices, which will open these practices up to additional regulator and investor scrutiny. While this additional scrutiny may be warranted in some circumstances, what is certain is that the amended rules will prompt companies to spend additional time and resources examining their internal practices in this area and potentially adopt changes.

These amendments, specifically the prescriptive cooling-off periods, may make Rule 10b5-1 plans less attractive to corporate insiders, which may prove to further limit the ability of officers and directors to execute trades in their companies' securities.

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