

# SEC Reporting & Compliance Alert

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**Editor's note:** This client alert was updated on January 26, 2023, to include additional information about compliance deadlines, which is reflected in the table at the end of the article.

## SEC Amends Rules for Rule 10b5-1 Trading Plans and Adds New Disclosure Requirements

On December 14, 2022, the U.S. Securities and Exchange Commission (SEC) adopted several amendments and new disclosure requirements intended to address what it perceives may be abusive practices relating to Rule 10b5-1 trading plans, certain equity awards and gifts of securities. Significant new provisions include:

- “cooling-off” periods delaying the first trades after a plan is adopted or amended;
- limitations on the number of Rule 10b5-1 plans an insider may have and on single-trade arrangements; and
- new required disclosures by issuers about Rule 10b5-1 plans, insider trading policies and option grant practices.

Notably, the amendments do not address issuer Rule 10b5-1 plans for share repurchases by issuers. The SEC proposed rules on issuer share repurchases in December 2021,<sup>1</sup> and final rules are expected to be adopted in 2023.

### Amendments to Rule 10b5-1

Rule 10b5-1 under the Securities Exchange Act of 1934 (Exchange Act) provides an affirmative defense to insider trading for individuals and issuers that trade stocks under plans entered into in good faith at a time when the individual or issuer does not possess material nonpublic information. The amendments add new conditions that also must be satisfied to avail oneself of the affirmative defense:

### Cooling-off Period

The amendments will require a minimum “cooling-off period” between the date a Rule 10b5-1 trading plan is adopted or modified and when trading under the plan commences.<sup>2</sup>

<sup>1</sup> See our December 21, 2021 client alert, “SEC Announces Proposals Relating to Rule 10b5-1, Share Repurchases and Other Matters.”

<sup>2</sup> Modifications that do not change the sales or purchase prices or price ranges, the amount of securities to be sold or purchased or the timing of transactions under a Rule 10b5-1 trading plan will not trigger a new cooling-off period. Examples of such non-triggering modifications include an adjustment for stock splits or a change in account information.

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*Directors and officers.* With respect to directors and officers,<sup>3</sup> the applicable cooling-off period is the later of (i) 90 days after the adoption or modification of the trading plan or (ii) two business days following the filing of the Form 10-Q or Form 10-K for the fiscal quarter in which the plan was adopted or modified. In any event, the required cooling-off period is not to exceed 120 days following adoption or modification of the plan.

*Other persons.* With respect to persons other than issuers, directors or officers, the applicable cooling-off period is 30 days after the adoption or modification of the trading plan.

The SEC refrained for now from adopting a cooling-off period for issuers' share repurchase plans, and is still considering whether one is warranted.

## Director and Officer Representations

When adopting a new or modified Rule 10b5-1 trading plan, a director or officer will be required to include in the plan written representations certifying that he or she (i) is not aware of material nonpublic information about the issuer or its securities and (ii) is adopting or modifying the plan in good faith and not as part of a plan or scheme to evade the prohibitions of Exchange Act Rule 10b-5.

## Prohibitions Against Multiple, Overlapping Plans

Persons, other than issuers, generally will be prohibited from having more than one Rule 10b5-1 trading plan for open market purchases or sales of an issuer's securities.

This prohibition does not apply where a person transacts directly with the issuer, such as participating in employee stock ownership plans (ESOPs) or dividend reinvestment plans (DRIPs), which are not executed on the open market. Also, the prohibition does not apply to plans authorizing an agent to sell only enough securities as are necessary to satisfy tax withholding obligations arising exclusively from the vesting of a compensatory award, such as on the vesting and settlement of restricted stock units ("sell-to-cover" Rule 10b5-1 plans), provided that the award holder is not permitted to exercise control over the timing of such sales.<sup>4</sup>

The amendments also make clear that a series of separate contracts with different broker-dealers to execute trades pursuant to a single Rule 10b5-1 trading plan would be treated as a single plan.

Also, a person, other than an issuer, may maintain two separate Rule 10b5-1 plans for open market purchases or sales of an

issuer's securities if trading under the later-commencing plan is not authorized to begin until after all trades under the earlier-commencing plan are completed or expire without execution. If the first plan is terminated early, the first trade under the later-commencing plan, however, must not be scheduled to occur until after the effective cooling-off period following the termination of the earlier plan.

## Limitations on Single-Trade Arrangements

In any 12-month period, a person other than an issuer is limited to one "single-trade plan" — one designed to effect the open market purchase or sale of the total amount of the securities subject to the plan as a single transaction.

A plan will not be treated as a single-trade plan if, for example, it gives the person's agent discretion over whether to execute the plan as a single transaction, or provides that the agent's future acts will depend on events or data not known at the time the plan is entered into and it is reasonably foreseeable at the time the plan is entered into that the plan might result in multiple trades. Also, sell-to-cover Rule 10b5-1 plans are exempt from this limitation.

As with the cooling-off period, the SEC refrained for now from adopting prohibitions against multiple, overlapping plans and applying limitations to single-trade plans for issuers, and is still considering whether those are warranted.

## Expanded Good Faith Requirement

The current Rule 10b5-1 requires that plans be entered into in good faith. The amendments add to that a requirement that the person who entered into the Rule 10b5-1 plan "has acted in good faith with respect to" the plan, thus extending the good faith requirement throughout the duration of the plan. As an example, the SEC notes that influencing the timing of an issuer's disclosure so that trades under a plan are more profitable would run afoul of this ongoing good faith requirement.

The amendments would not affect the affirmative defense available under a Rule 10b5-1 plan that was entered into prior to the amendment's effective date, unless that plan is modified after the effective date of the amendments.

## Issuer Disclosures

The amendments introduce the following new disclosure requirements for issuers:

### Insider Trading Policies and Procedures Exhibit

Under new Regulation S-K Item 408(b), an issuer will be required to disclose on Form 10-K or in the annual meeting proxy statement whether it has adopted insider trading policies

<sup>3</sup> "Officers" refer to those defined in Exchange Act Rule 16a-1(f), also known as section 16 officers, for purposes of these rules.

<sup>4</sup> This exemption does not apply to sales incident to the exercise of option awards, because the person exercising the option controls the timing of such sales.

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and procedures governing the purchase, sale and/or other dispositions of the issuer's securities by directors, officers and employees, or the issuer itself, that are reasonably designed to promote compliance with insider trading laws, rules and regulations, as well as applicable listing standards. If it has, it will be required to file a copy of them as an exhibit to its annual report on Form 10-K. If no such policies or procedures are in place, the issuer will need to explain why.

Foreign private issuers will be required to provide analogous disclosure, including filing a copy of their insider trading policies and procedures as an exhibit, in their annual reports pursuant to new Item 16J in Form 20-F.

## Adoption, Modification and Termination of Rule 10b5-1 Plans and Certain Other Trading Arrangements

Under new Regulation S-K Item 408(a), issuers will be required to provide quarterly disclosure on Forms 10-Q and 10-K of (i) whether any director or officer has adopted, modified or terminated a Rule 10b5-1 plan or non-Rule 10b5-1 trading arrangement<sup>5</sup> and (ii) a description of the material terms of each plan, including the name and title of the director or officer; the date the plan was adopted, modified or terminated; the plan's duration; and the total amount of securities to be purchased or sold under the plan. Issuers will not be required to disclose pricing terms.

The SEC refrained for now from requiring corresponding disclosures from issuers about their trading arrangements and is still considering whether such disclosure requirements are warranted.

## Options Granted Close in Time to the Release of Material Nonpublic Information

Under new Regulation S-K Item 402(x), issuers (including smaller reporting companies and emerging growth companies) will be required to disclose on Form 10-K or in the annual meeting proxy statement the issuer's policies and practices regarding the timing of awards of options in relation to the disclosure of material nonpublic information.<sup>6</sup> Issuers will need to discuss (i) how the timing of awards is decided, (ii) how material nonpublic information is considered, if at all, when determining the timing and terms of awards, and (iii) whether disclosure of such information is timed to affect the value of awards.

Issuers also will be required to disclose in a new table any

<sup>5</sup> A "non-Rule 10b5-1 trading arrangement" is defined in new Regulation S-K Item 408(c), and includes certain pre-planned trading arrangements that do not meet the conditions of the Rule 10b5-1(c)(1) affirmative defense.

<sup>6</sup> The term "option" is defined in Regulation S-K Item 402(a)(6) and includes stock options, stock appreciation rights (SARs) and similar instruments with option-like features.

options granted in the last completed fiscal year to named executive officers that were granted within four business days before or one business day after the (i) filing of a periodic report on Form 10-Q or 10-K or (ii) filing or furnishing of a current report on Form 8-K that contains material nonpublic information (other than disclosure of a material new option award grant under Form 8-K Item 5.02(e)). The table would provide the following:

- each award (including the grantee's name, the number of securities underlying the award, the date of the grant, the grant-date fair value and the option's exercise price); and
- the percentage change in market price of the securities underlying each award on the trading day before and after disclosure of the material nonpublic information.

## Inline XBRL Tagging

The amendments will require issuers to tag the information specified by new Regulation S-K Items 402(x), 408(a) and 408(b)(1) in Inline XBRL.

## Section 16 Reporting

The amendments will impose the following new disclosure requirements for Section 16 filers:

### Rule 10b5-1 Checkbox

A mandatory checkbox will be added to Forms 4 and 5, where filers will have to indicate whether a transaction reported on that form was made under a plan intended to satisfy the affirmative defense conditions of Rule 10b5-1. If so, filers would need to provide the date the plan was adopted.

### Gifts

Bona fide gifts of equity securities would no longer be reported on Form 5, but instead would have to be reported on Form 4 and filed before the end of the second business day following the date of the gift. Acquisitions of gifts are still eligible to be reported on a Form 5 or any time earlier on a Form 4, voluntarily.

## Next Steps

Issuers should consider what controls and processes will be necessary to enable them to make the new disclosures required under the rules.

Issuers also may want to assess the various circumstances in which their insiders utilize the affirmative defense of existing Rule 10b5-1 plans and plan for timing and other changes — including, if necessary, amending their Rule 10b5-1 policies and guidelines — that will be required in light of the new rules.

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Finally, issuers may want to review their compensation committee calendar to consider whether it needs to be revised in light of the new disclosure rules applicable to options granted close in time to the release of material nonpublic information.

## Transition Periods / Effective Date

Final Rules	Compliance Date	First Filing for 12/31 Fiscal Year-End Issuers
Amendments to Rule 10b5-1	Rule 10b5-1 plans entered into, or modified, on or after February 27, 2023	N/A
Gift Reporting (Exchange Act Rule 16a-3)	Dispositions by gift made on or after February 27, 2023, are reportable on Form 4 within two business days	N/A
Amendments to Forms 4 and 5	Forms 4 or 5 filed on or after April 1, 2023	N/A
Disclosure of Adoption, Modification or Termination of Rule 10b5-1 Plans by Directors or Officers (Reg. S-K Item 408(a))	The first filing that covers the first full fiscal quarter beginning on or after April 1, 2023 <sup>7</sup>	Form 10-Q for quarter ending June 30, 2023 <sup>8</sup>
Disclosure of the Issuer's Insider Trading Policies and Procedures (Reg. S-K Item 408(b)(1); Form 20-F Item 16J)	The first filing that covers the first full fiscal year beginning on or after April 1, 2023 <sup>7</sup>	Proxy Statement for 2025 Annual Meeting (or Form 10-K or 20-F for fiscal year ending December 31, 2024) <sup>9</sup>
Insider Trading Policies and Procedures Exhibit (Reg. S-K Items 408(b)(2) and 601(b)(19); Form 20-F Item 16J)	The first filing that covers the first full fiscal year beginning on or after April 1, 2023 <sup>7</sup>	Form 10-K or 20-F for fiscal year ending December 31, 2024 <sup>9</sup>
Tabular and Narrative Disclosure of Certain Options Awarded Close in Time to the Release of Material Nonpublic Information and Related Policies and Procedures (Reg. S-K Item 402(x))	The first filing that covers the first full fiscal year beginning on or after April 1, 2023 <sup>7</sup>	Proxy Statement for 2025 Annual Meeting (or Form 10-K for fiscal year ending December 31, 2024) <sup>9</sup>

<sup>7</sup> October 1, 2023, for smaller reporting companies.

<sup>8</sup> Form 10-K for fiscal year ending December 31, 2023, for smaller reporting companies.

<sup>9</sup> Although this delayed reporting appears it may not have been intended when the SEC adopted the amendments, we confirmed with the SEC staff that it is correct.

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