

SEC Adopts New Restrictions on 10b5-1 Plans,? Related Disclosure Requirements and Section 16 Filing Changes

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On December 14, 2022, the SEC unanimously adopted cooling-off periods and other changes to how plans adopted under Rule 10b5-1 (“10b5-1 Plans”) will work going forward. Executive officers and directors of public companies frequently use 10b5-1 Plans to conduct sales of their company’s stock at a time when they have material non-public information (“MNPI”) about the company or its securities, which is permitted if they entered into the plan at a time that they did not have MNPI and gave up control over the sales. The new rule changes require additional disclosures about 10b5-1 Plans in the issuer’s SEC filings, as well as include some changes to the short-swing profit recapture rules and required filings under Section 16 of the Securities Exchange Act.

The unanimous approval by the SEC Commissioners (see the Adopting Release [here](#)) followed some significant easing of requirements in the proposed rules initially issued last December (see the Proposing Release [here](#)), particularly by excluding 10b5-1 Plans of issuers themselves from application of the new rules.

Rule 10b5-1 Plan Amendments

The amendments to the Rule 10b5-1(c)(1) affirmative defense to insider trading liability include:

Cooling-off Periods:

10b5-1 Plans of executive officers and directors may not permit sales (or purchases) until the later of (1) 90 days following the adoption of the plan and (2) two business days following disclosure of the issuer’s financial results on Form 10-Q or Form 10-K, as applicable, for the fiscal quarter in which the plan was adopted, but not to exceed 120 days after adoption. Modifying a 10b5-1 Plan results in a new cooling-off period.

10b5-1 Plans of others (excluding the issuer) may not permit sales (or purchases) for 30 days after adoption or modification. For example, this limitation would apply to employees who are not executive officers.

No cooling-off period is required for 10b5-1 Plans adopted by issuers.

Other Conditions:

The rule changes add a requirement that executive officers and directors certify to the issuer that they are not aware of MNPI at the time of entering into or modifying a 10b5-1 Plan and that they are adopting the plan in good

faith and not as a part of a plan or scheme to evade the rules. In practice, most broker-dealer standard forms already included similar certifications.

The rule changes also specify that a person entering into a 10b5-1 Plan must have acted in good faith in using the plan to be eligible for the affirmative defense.

The rule changes exclude from the protection of Rule 10b5-1, with respect to any class of issuer securities, multiple overlapping 10b5-1 Plans and more than one single-trade 10b5-1 Plan in any 12-month period. Section 16 insiders will be required to check a box on their Form 4 and Form 5 filings to indicate whether the transactions were intended to be Rule 10b5-1 transactions and the date of adoption of the applicable 10b5-1 Plan.

New Issuer Disclosure Requirements

Companies must make annual disclosure of whether or not they have adopted insider trading policies and procedures (with copies required to be filed as exhibits to the Form 10-K). They must also make quarterly disclosure of any 10b5-1 Plans and other written trading arrangements used by their executive officers and directors, by providing a description of the material terms of the 10b5-1 Plans, including:

- the name and title of the director or executive officer;
- the date of adoption or termination of the 10b5-1 Plan;
- its duration; and
- the aggregate number of securities to be sold or purchased.

There is no requirement to disclose terms relating to the price at which the broker-dealer effecting trades under the 10b5-1 Plan is authorized to trade.

As part of their annual executive compensation disclosure, companies must make additional disclosures about stock option awards made close in time to the release of MNPI. The rule changes will require XBRL tagging of some of the disclosures.

Bona Fide Gifts of Stock Trigger Form 4 Filing

Currently, a Section 16 insider may make charitable contributions or other gifts of stock without reporting the gift until the Form 5 filing deadline 45 days after the fiscal year in which the gift is made. The rule changes will require Section 16 insiders to report gifts on Form 4 within two business days of the gift.

Effective Dates of the Rule Changes

The rule changes take effect 60 days after publication of the adopting release in the Federal Register, or February 27, 2023. This includes the requirement to report gifts on Form 4.

The new disclosure requirements will apply to companies beginning with the first filing that covers the first full fiscal period that begins on or after April 1, 2023, so for calendar year U.S. companies, typically with the second-quarter Form 10-Q in the summer of next year. Smaller reporting companies get an additional six months before

the rule changes apply to them.

The Form 4 changes? relating to identification of 10b5-1 transactions ?will apply to filings on or after April 1, 2023.

Takeaways

- Executive officers and directors will want to take into account the consequences of the new cooling-off periods when considering sales of stock to diversify their holdings or to anticipate future expenses? and determine whether it is necessary or desirable to use a 10b5-1 Plan for the sale at all.
- Broker-dealers will need to update their standard forms for 10b5-1 Plans to reflect the changes.
- Companies should consider adopting a pre-clearance procedure (if they do not already use one) so that they will obtain information from their executive officers and directors about any new or modified 10b5-1 Plans.
- Companies should consider updating their policies covering trading in the company's stock to reflect the changes.
- Companies should also consider updating the manuals they provide executive officers and directors that describe Section 16 filing requirements and 10b5-1 Plans and providing related training to reflect the new requirements, particularly the Form 4 filing requirement for gifts.
- Companies that now require use of 10b5-1 Plans for insider ?transactions may want to revisit the extent to which such requirement should be continued in ?view of the new cooling-off periods and enhanced disclosure requirements.?
- Companies may want to revisit the timing of their grants of stock options or add an internal guideline to check on timing of release of any MNPI before making those grants.

If you have any questions about these changes, your regular Locke Lord contact or any of the authors can discuss these matters with you.

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