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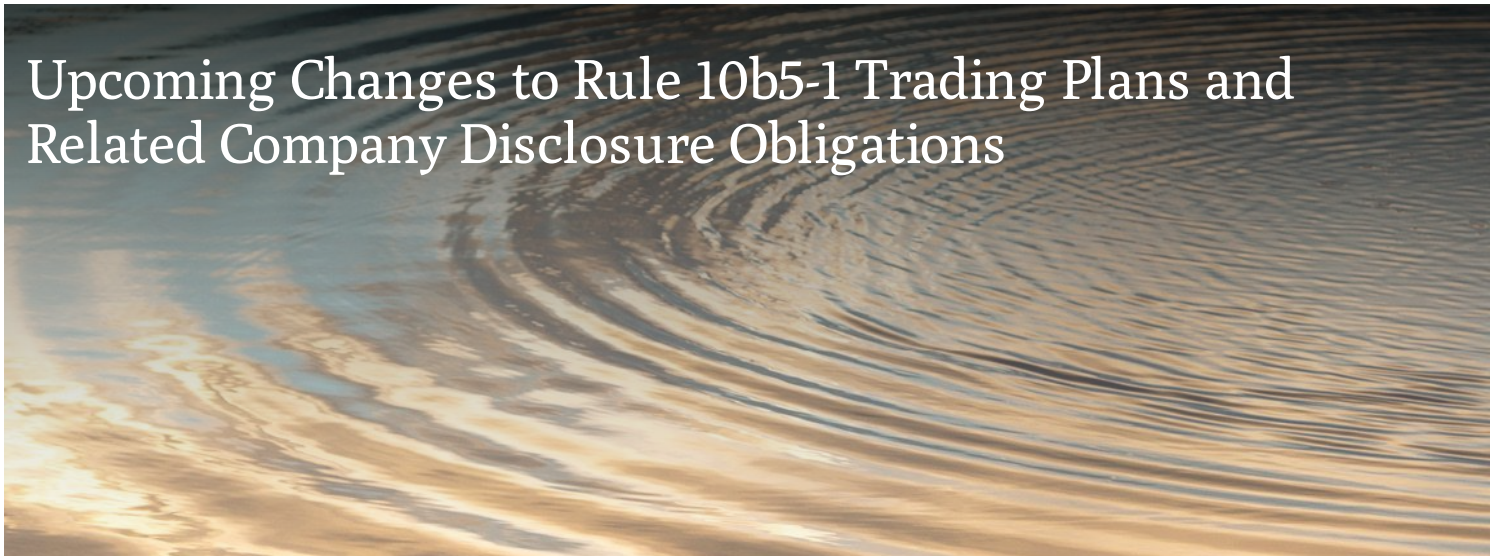

Upcoming Changes to Rule 10b5-1 Trading Plans and Related Company Disclosure Obligations

FEBRUARY 1, 2022

Rule 10b5-1 trading plans in essence provide corporate insiders an affirmative defense to insider trading liability in circumstances where, subject to certain conditions, a trade was executed pursuant to a written plan adopted when the executive was not aware of material nonpublic information. Executive officers and directors are not required to complete trades using 10b5-1 plans, but they are quite popular with executive officers and directors because of the protection they provide.

To address concerns regarding the perceived abuse by insiders of 10b5-1 plans to "opportunistically trade securities on the basis of material nonpublic information", in mid-December 2021, the SEC proposed amendments to Rule 10b5-1 under the Securities Exchange Act to add new conditions to the availability of the affirmative defense under the rule, including:

- A 120-day cooling-off period before trading can begin following adoption or modification of a trading plan;
- A requirement that officers and directors certify in writing that they are unaware of material nonpublic information when entering into a new or modified trading plan;
- A prohibition on overlapping trading plans (to prevent the potentially abusive practice of using overlapping plans with selective cancellation of certain plans or trades on the basis of material nonpublic information);
- A limit on single-trade plans to one per 12-month period (with the SEC noting that "research suggests that insiders using single-trade plans may be executing trades based on material nonpublic information"); and
- Expansion of the existing good-faith requirement for trading under the plan to require that a plan be "operated" in good faith in addition to the existing requirement that the plan be "entered into" in good faith.

If these amendments are approved as proposed, executives will need to factor in these new requirements when implementing 10b5-1 plans.

Also noteworthy is that the proposed amendments would impose new requirements on issuers that would significantly expand disclosures regarding issuer insider-trading policies and procedures, Rule 10b5-1 trading arrangements, and option grants, including:

- A requirement to disclose in the company's annual reports whether it has insider-trading policies and procedures (if yes, describe; if no, explain why not);
- A requirement to disclose in the company's quarterly reports the adoption and termination (including modification) of Rule 10b5-1 trading arrangements and other trading arrangements by directors, officers, and issuers, and the terms of such trading arrangements;
- A requirement that Section 16 officers and directors disclose on Forms 4 and 5 whether a reported transaction was made pursuant to a 10b5-1(c) trading arrangement; and
- A requirement for the company to disclose in its annual reports its grant policies and practices with respect to options, SARs, and similar instruments, and to provide tabular disclosure showing grants of options, SARS, or similar instruments made within 14 days of the release of material nonpublic information and the market price of the underlying securities on the trading day before and after the release of such information.

Winston Takeaway. The SEC requested comments on multiple (72!) aspects of the proposed amendments, but we anticipate that the rules will be finalized in substantially the form proposed. As a result, public companies should become familiar with the proposed amendments, and begin thinking about how they will comply with the proposed new requirements, including (i) reviewing insider-trading policies in light of proposed new disclosure rules, (ii) reviewing equity grant practices (particularly companies that grant options and option-like awards), and (iii) reviewing and considering enhancements to disclosure controls and procedures to comply with proposed new reporting requirements.

Please contact a member of the Winston & Strawn Employee Benefits and Executive Compensation Practice Group, Capital Markets Practice Group, or your Winston relationship attorney for further information.

Winston & Strawn Paralegal Kristine Lofquist also contributed to this blog post.
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Authors

Joseph S. Adams

David A. Sakowitz

Kevin Smith

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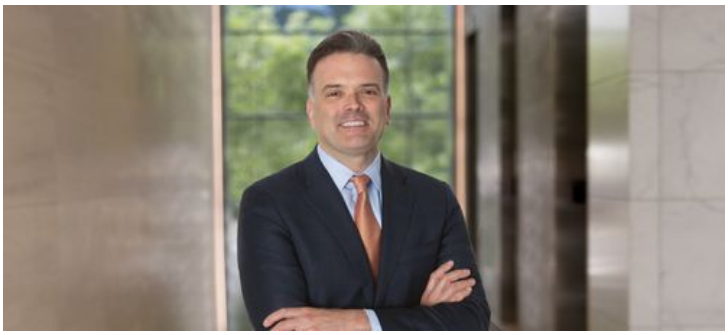

Joseph S. Adams

David A. Sakowitz

Kevin Smith

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