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Meridian Client Update

SEC Issues Proposed Rules on 10b5-1 Trading Plans and Share Buybacks

On December 15, 2021, the Securities and Exchange Commission (SEC) proposed rules that would impose: (i) new conditions for Rule 10b5-1 trading plans; (ii) new disclosure requirements on trading plans and securities transactions by companies and insiders; and (iii) new disclosure requirements related to company share repurchases.

Proposed Rules	Current Rules
▪ **Impose the following new conditions on Rule 10b5-1 trading plans:**	
— Mandate significant delays between trading plan adoption, modification or termination and initial trades	Do not impose a trading delay
— Prohibit multiple overlapping trading plans and restrict single-trade plans	Do not prohibit overlapping trading plans or restrict single trade plans, except in certain narrow circumstances
— Require officers and directors to personally certify that they are not aware of material nonpublic information when they adopt a trading plan	Do not require such certification
▪ **Require companies to meet new disclosure rules covering the following matters:**	
— Rule 10b5-1 trading plans and other trading arrangements	Do not include mandated disclosures of trading plans
— Insider trading policies and procedures	Do not require a company to disclose its insider trading policies or procedures
— Timing of stock option grants	May require a company to disclose in its Compensation Discussion and Analysis information about the timing of option grants in close proximity to the release of material nonpublic information by the company

Proposed Rules	Current Rules
▪ **Require public companies to disclose the following additional details regarding share buybacks:**	Require a public company to disclose on a quarterly basis any purchase made by or on behalf of the public company, or any affiliated purchaser, of shares or other units of any class of the public company's registered equity securities
– The details of a share repurchase on new Form SR which must be furnished to the SEC no later than the end of the first business day following the day on which a share repurchase occurred	
– The objective/rationale (among other items) of its share repurchase program	
– Whether any Section 16 officer or director purchased or sold company shares that are subject to share repurchase plan	

The SEC requests that comments on the proposed rules be submitted no later than 45 after the proposed rules are published in the Federal Register, which we expect to occur in the coming days.

Meridian comment. **The SEC is under no obligation to adopt a final rule within a specified period following the conclusion of the comment period. However, the SEC is not likely to drag its feet on the proposed rules given SEC Chair Gary Gensler's previously stated interest in this area (see Meridian Client Update dated June 18, 2021). We anticipate that the SEC is likely to adopt final rules on both Rule 10b5-1 trading plans and share repurchases in the near-term. Companies should start reviewing the design of 10b5-1 plans adopted by executives and directors, as well as their insider trading policies and procedures.**

The proposed rules are summarized below.

Proposed Amendments to Rule 10b5-1 (imposition of new conditions on trading plans)

The nature and purpose of trading plans under current Rule 10b5-1 and the new conditions that would be imposed on trading plans under the proposed amendments are discussed below.

Background on Trading Plans

Rule 10b-5 prohibits securities fraud, including insider trading through the purchase or sale of securities on the basis of material nonpublic information. Rule 10b5-1, which was adopted in 2000, allows insiders (e.g., officers and board members) to transact in their company's securities by establishing prearranged trading plans. Rule 10b5-1 trading plans provide an **affirmative defense to insider trading allegations** if the plan is entered into: (i) in good faith; (ii) while the individual or public company is unaware of any material nonpublic information; (iii) with specifications regarding the number of securities, price and date of future transactions or a formula for making such determinations; and (iv) with prohibitions on exercising any subsequent influence over any person executing the plan.

Rule 10b5-1 provides an affirmative defense designed to demonstrate that a purchase or sale was not made "on the basis of" material nonpublic information. The rule provides a safe harbor for "insiders" (i.e., executives and directors) who are buying or selling company stock, as well as public companies that repurchase shares through buyback programs, to make trades during periods where they are aware of material nonpublic information or during "black-out" periods during which trading is otherwise prohibited. As

a result, many executives have adopted Rule 10b5-1 trading plans that govern the sale of their company securities.

When properly administered, Rule 10b5-1 trading plans benefit both executives and companies by reducing the risk of litigation alleging insider trading, making it easier for companies to administer their stock programs, and, perhaps most importantly, allowing executives to diversify their assets while not sending unintended signals to the market.

Proposed Conditions on Trading Plans

The SEC's proposed amendments to Rule 10b5-1, if adopted, would impose the following new conditions on trading plans:

- Mandate delays between trading plan adoption, modification or termination and initial trades ("Cooling-off Period").
- Prohibit multiple overlapping trading plans and restrict single-trade plans.
- Require officers and directors to personally certify that they are not aware of material nonpublic information about their company when they adopt a trading plan.

These proposed rule amendments are described below.

Mandatory Cooling-off Period

The proposed amendments to Rule 10b5-1 would impose the following mandatory delay period between a plan adoption or modification and initial trades:

- Officers and directors would be prohibited from trading for a 120-day period after adopting a new trading plan or modifying an existing trading plan
- Public companies would be prohibited from trading for a 30-day period after adopting a new trading plan or modifying an existing trading plan.[1]

Cancellation of one or more trades or termination of a plan would constitute a modification to an existing plan.

After the cooling-off period has ended, trading could commence after a company announces its next quarterly financial results. The release to the proposed rule ("Release") notes that "[t]he length of the proposed cooling-off period would deter insiders from seeking to capitalize on unreleased material nonpublic information for the upcoming quarter." The Release also states that these restrictions will discourage the selective cancellation of trading plans or trades on the basis of material nonpublic information.

[1] Public companies use 10b5-1 trading plans when repurchasing their shares through open market purchases, tender offers, private negotiated transactions, and accelerated share repurchases.

Prohibition on Multiple Overlapping Trading Plans and Restriction on Single-Trade Plans

The proposed amendments to Rule 10b5-1 would impose the following new restrictions on overlapping and single trade trading plans:

- Officers and directors would be prohibited from implementing multiple overlapping plans for open market trades in the same class of securities, and
- Officers and directors would be allowed to use single-trade plans only once during any consecutive 12-month period.

The Release notes that these proposed restrictions are intended to preclude officers and directors from using a trading plan to strategically schedule and execute trades based on material nonpublic information.

Officer and Director Certification

The proposed amendment to Rule 10b5-1 would require an officer or director to certify the following at the time that the officer or director adopts a trading plan:

- The person is not aware of material nonpublic information about the company or its securities.
- The person is adopting the plan in good faith and not as part of a plan or scheme to evade Section 10(b) of the Securities Exchange Act of 1934 ("Exchange Act").

The proposed certification would not provide an independent basis of liability for directors or officers under Section 10(b) or Rule 10b-5. Rather, the Release notes, the proposed certification would "underscore certifiers' awareness of their legal obligations under the federal securities law related to the trading in the public company's securities."[2]

A director or officer should retain a copy of the certification for a period of ten years. The ten-year period corresponds with the statute of limitations that governs the SEC's ability to seek certain remedies for insider trading claims.

New Disclosure Requirements

The proposed rules would require companies to disclose information about the following items:

- Rule 10b5-1 trading plans and other trading arrangements.
- Insider trading policies and procedure.
- Timing of stock option grants.

[2] To prevail in a securities fraud claim under Section 10(b) of the Exchange Act, a plaintiff must allege and prove that the defendant acted with knowledge of wrongdoing. A false certification would be evidence that an officer or director acted with such intent.

Rule 10b5-1 Trading Plan New Disclosure Requirement

The proposed rules would require companies to quarterly disclose the following information on Form 10-Q and Form 10-K:

- Whether the company, a director or an officer has adopted, modified or terminated a Rule 10b5-1 plan or another trading arrangement during the last fiscal quarter.
- The person's name and title (if applicable).
- The date of adoption or termination.
- The plan's duration.
- The aggregated amount of securities to be sold or purchased pursuant to the plan.

Insider Trading Policies and Procedures Disclosure Requirement

The proposed rules would require companies to annually disclose in Form 10-Ks and in proxy statements their insider trading policies and procedures (or lack thereof and the rationale for not having adopted such policies and procedures).[3] The Release notes that a company's disclosure may include the following information:

- The company's process for:
  - — Assessing whether insiders or the company itself has material nonpublic information at the time of trading activity.
  - — Documenting such determinations.
  - — Approving requests to purchase or sell its securities.
- The company's method of enforcing compliance with its insider trading policies and procedures.

Disclosure Requirement Related to the Timing of Stock Option Grants

The proposed rules would require companies to disclose the following information on the timing of stock option grants in tabular format:

- Each stock option or stock appreciation right (SAR) granted within 14 calendar days before or after: (i) the filing of a periodic report; (ii) a public company's share repurchase; or (iii) the filing or furnishing of a Form 8-K that contains material nonpublic information.
- The number of shares underlying the option or SAR award, the date of grant, the exercise price and the grant date fair value.
- The company's stock prices on the trading days before and after disclosure of the material nonpublic information.

The proposed 14-day window is designed to cover the period that a company would be aware of material nonpublic information at the time that its board of directors grants an option award.

[3] Foreign private issuers would be required to disclose their insider trading policies and procedures on Form 20-F.

In addition, the proposed rules would require narrative disclosure regarding the company's option grant policies and practices regarding the timing of option grants and the release of material nonpublic information. Such disclosure would be required to include the following information:

- How the board of directors determines when to grant options.
- Whether and, if so, how, the board of directors or compensation committee takes material nonpublic information into account when determining the timing and terms of an award.

The proposed rules would require the above disclosures to be included in a company's annual report on Form 10-K and annual proxy statements. Companies would generally be required to include the proposed narrative disclosure in its CD&A.[4]

Share Repurchase Disclosure Modernization

On December 15, 2021, the SEC issued proposed rules that would update the disclosure requirements on share buybacks by public companies.

Current Rules

Currently, a public company is required to disclose on a quarterly basis any purchase made by or on behalf of the public company or any affiliated purchaser of shares or other units of any class of the public company's equity securities registered under Section 12 of the Exchange Act. This disclosure requirement applies to both open market and private transactions. Share repurchase disclosure is required in Form 10-Q for repurchases made during a public company's first three fiscal quarters and in Form 10-K for repurchases made during a public company's fourth quarter.

Proposed Rules

In the release to the proposed rule, the SEC expressed concern that "because [public companies] are repurchasing their own securities, asymmetries may exist between companies (and affiliated purchasers) and investors with regard to information about the public company and its future prospects. This, in turn, could exacerbate some of the potential harms associated with public company repurchases." To help address these information asymmetries, the SEC is proposing a new disclosure form and additional disclosure requirements about public company repurchases.

The proposed rules would require a company to disclose the following information regarding repurchases of a public company's equity securities:

- Daily repurchases on a new Form SR, which would be furnished to the Commission one business day after execution of a public company's share repurchase order; and
- Additional detail regarding the structure of a public company's repurchase program and its share repurchases.

Proposed Form SR

The SEC is proposing new Rule 13a-21 and Form SR that would require a public company, including a foreign private issuer and certain registered closed-end funds, to report any purchase made by or on behalf of the public company or any affiliated purchaser of shares or other units of any class of the public company's equity securities that is registered. The public company would have to furnish a new Form SR before the end of the first business day following the day on which the public company executes a share

[4] Emerging growth companies and smaller reporting companies would be required to include the disclosures on the timing of stock option grants in their proxy statements, even though they are subject to scaled executive compensation disclosures.

repurchase. The Form SR would require the following disclosures for each class or series of securities subject to repurchase:

Date	(a) Class of Shares	(b) Total Number of Shares Purchased	(c) Average Price Paid per Share	(d) Total Number of Shares Purchased on the Open Market	(e) Total Number of Shares Purchased in Reliance on the Safe Harbor in 17 CFR 240.10b-18	(f) Total Number of Shares Purchased Pursuant to a Plan that is Intended to Satisfy the Affirmative Defense Conditions of 17 CFR 240.10b5-1(c)[5]

The SEC notes that the form is not to be used as a blank form to be filled in, but should be used as a guide in the preparation of the report meeting the requirements of proposed Rule 13a-21.

The proposed rule would require public companies to furnish, rather than file, Form SR. As a result, public companies *would not* be subject to liability under certain anti-fraud provisions of the Exchange Act[6] for the disclosure in the form. In addition, the information would not be deemed incorporated by reference into filings under the Securities Act of 1934 ("Securities Act") and thus *would not* be subject to liability under Section 11 of the Securities Act[7], unless the public company expressly incorporated such information.

Proposed Revision to Item 703 - Additional Disclosure[8]

The SEC is proposing to revise Item 703, including corresponding changes to Form 20-F and Form N-CSR, to require additional disclosure about a public company's share repurchases. Specifically, the proposed revisions would require a public company to disclose:

- The objective or rationale for its share repurchases and process or criteria used to determine the amount of repurchases;
- Any policies and procedures relating to purchases and sales of the public company's securities by its officers and directors during a repurchase program, including any restriction on such transactions;
- Whether it made its repurchases pursuant to a plan that is intended to satisfy the affirmative defense conditions of Rule 10b5-1(c)[9], and if so, the date that the plan was adopted or terminated; and
- Whether purchases were made in reliance on the Rule 10b-18 non-exclusive safe harbor[10].

[5] Column f of the proposed table refers to the safe harbor from liability for share repurchases by an issuer under a Rule 10b5-1 trading plan.
[6] Specifically, Section 18 of the Exchange Act, which imposes liability on any person who shall make or cause to be made any false and misleading statement of material fact in any application, report, or document filed under the Act.
[7] Sections 11(a) and (b) of the Securities Act provide for strict liability for issuers who make material misstatements or omissions in the issuance of securities.
[8] The SEC is also proposing clarifying amendments to Item 703, Form 20-F and Form N-CSR to simplify application of the rules and remove unnecessary instructions.
[9] Rule 10b5-1(c) provides a safe harbor from liability for trades made under a Rule 10b5-1 trading plan.
[10] Rule 10b-18 provides an issuer a safe harbor from liability under certain market manipulation rules and Exchange Act Rule 10b-5 when repurchases of the issuer's common stock satisfy the rule's conditions.

In addition, under the SEC proposed rule, public companies would be required to include a tabular disclosure indicating if any of their Section 16 officers or directors purchased or sold shares or other units of the class of the public company's equity securities that are the subject of a public company share repurchase plan or program, within 10 business days before or after the announcement of the plan or program. Public companies would also be required to disclose the following in a footnote to the table or narrative accompanying the table:

- The objective or rationale for each repurchase plan or program and the process or criteria used to determine the amount of repurchases.
- The number of shares purchased.
- For publicly announced repurchase plans or programs:
  - — The date each plan or program was announced;
  - — The dollar amount (or share or unit amount) approved;
  - — The expiration date (if any) of each plan or program;
  - — Each plan or program that has expired during the period covered by the table; and
  - — Each plan or program the public company has determined to terminate prior to expiration, or under which the public company does not intend to make further purchases.
- Any policies and procedures relating to purchases and sales of the public company's securities by its officers and directors during a repurchase program, including any restrictions on such transactions.

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The ***Client Update*** is prepared by Meridian Compensation Partners' Governance and Regulatory Team led by Donald Kalfen. Questions regarding this Client Update or executive compensation technical issues may be directed to Donald Kalfen at 847-235-3605 or dkalfen@meridiancp.com.

www.meridiancp.com