

Securities Regulation Daily Wrap Up, TOP STORY—House starts year by passing insider trading bill, (Jan. 29, 2019)

Securities Regulation Daily Wrap Up

[Click to open document in a browser](#)

By [Mark S. Nelson, J.D.](#).

The House sent to the Senate a stand-alone version of insider trading legislation that, if enacted, could result in changes to Rule 10b5-1. The bill previously was part of JOBS Act 3.0 in the last Congress.

The House passed legislation that would require the SEC to study whether there are gaps in Exchange Act Rule 10b5-1 and to then conduct notice and comment rulemaking to close those gaps. The recently reintroduced Promoting Transparent Standards for Corporate Insiders Act ([H.R. 624](#)), sponsored by House Financial Services Committee Chairwoman Maxine Waters (D-Cal) and Ranking Member Patrick McHenry (R-NC) would bring new scrutiny to Rule 10b5-1 plans that are ostensibly used by corporate insiders to trade company stock without running afoul of the SEC's antifraud authorities. The JOBS Act 3.0 legislation that contained the insider trading bill passed the House overwhelmingly but faltered in the Senate in the last Congress. Questions remain about whether the new Senate will take up more House-passed financial bills than it did during the last Congress. The latest stand-alone version of the bill passed the House by a [vote](#) of 413-3.

Chairwoman Waters [told](#) members on the floor that Rule 10b5-1 has "several shortcomings" and that insider trading can erode confidence in securities markets. She also told members in [closing remarks](#) before the vote on the bill that the SEC needs additional resources to protect investors from fraud and that the SEC also needs "stability" following the recent government shutdown, which she said had left the SEC operating on a "skeleton crew" and could be repeated because the Trump Administration had not ruled out another shutdown when temporary government funding expires. Ranking Member McHenry [noted](#) the bipartisan character of the bill, which he said is the first bill from the House FSC in the 116th Congress. He told members that the bill is "critical for protecting mom-and-pop investors from the effects of insider trading" without also creating undue regulatory burdens.

NASAA, CII support insider bill. Michael S. Pieciak, Commissioner, Vermont Department of Financial Regulation and president of the North American Securities Administrators Association, [expressed support](#) for the bill. He said that NASAA encouraged passage because the bill would help prevent insider trading while furthering investor protection.

More specifically, Pieciak explained why the renewed focus on Rule 10b5-1 is needed. "As a practical matter, because all information related to Rule 10b5-1 trading plans is maintained by a corporation, insiders – i.e., the corporate officers or directors – are in effect policing themselves. It is comparatively easy for corporate insiders to manipulate the rule in order to engage in conduct that is tantamount to insider trading by, for example, belittling the potential materiality of nonpublic information or instituting trading plans that can be modified or cancelled prior to execution."

Likewise, the Council of Institutional Investors, in a [letter](#) to House FSC leaders, signaled its "strong support" for the bill, which it said would address some of the concerns the CII had raised in a 2012 [rulemaking petition](#) it submitted to the SEC. The CII's renewed interest and its rulemaking petition were, in part, prompted by a series of *The Wall Street Journal* articles that suggested corporate insiders were at least violating the "spirit" of Rule 10b5-1. Specifically, the CII petition cited executives' practices of: (1) adopting plans while they are aware of material, non-public information; (2) regularly amending or canceling plans; and (3) adopting plans that permit trading soon after adoption.

A more recent motivation for bringing forward legislation on Rule 10b5-1 plans arose following news reports that Intel Corporation CEO Brian Krzanich had exercised company stock options and sold the resulting shares pursuant to a modified Rule 10b5-1 [trading plan](#) in a time frame when Intel allegedly became aware of the Meltdown and Spectre cybersecurity vulnerabilities affecting Intel processors. That revelation prompted a January 2018 [letter](#) from Senate Banking Committee Members Jack Reed (D-RI) and John Kennedy (R-La) calling for SEC and Department of Justice investigations.

How the bill would work. Exchange Act Rule 10b5-1 specifies when securities trading is "on the basis of" material, nonpublic information regarding Exchange Act Section 10(b) and Rule 10b-5 which, in combination, constitute part of the SEC's most significant anti-fraud authorities. An affirmative defense exists to liability in three instances, including when a company executive adopts a written trading plan. However, such written trading plans must be entered into in good faith and cannot be entered into for the purpose of evading the requirements of Rule 10b5-1.

The Promoting Transparent Standards for Corporate Insiders Act would require the SEC to examine Rule 10b5-1 for gaps in coverage in light of insiders' current trading plan practices. Specifically, the SEC would have to consider whether to limit trading to issuer-adopted trading windows, to curb the use of multiple (the latest version drops the word "overlapping" as in "multiple, overlapping") trading plans, to mandate a delay between adoption of a trading plan and the first executed trade under the plan, to restrict an insider's ability to modify or cancel a trading plan, to require companies and insiders to make certain filings with the Commission, and to mandate that company boards adopt relevant policies and monitor for compliance.

The study also must consider factors such as whether revisions to Rule 10b5-1 would clarify existing limits on insider trading, alter companies' desire to be public companies, impact capital formation, or affect the ability to recruit executives. The Commission would have to report to Congress within one year of enactment and, upon completing the study, conduct a notice and comment rulemaking to revise Rule 10b5-1.

The text of the latest version is nearly identical to both the stand-alone ([H.R. 6320](#)) and JOBS Act 3.0 (Title XXVII) versions introduced in the 115th Congress. The JOBS and Investor Confidence Act of 2018 ([S. 488](#)) (aka JOBS Act 3.0) passed the House by a vote of 406-4, while the stand-alone version of the Rule 10b5-1 plan bill in the last Congress was reported by the House FSC but was not brought before the full House (See the following [White Paper](#) for addition analysis of the JOBS Act 3.0 Rule 10b5-1 provision at pages 9-10).

Companies: Intel Corporation

MainStory: TopStory CorporateGovernance CorpGovNews GCNNews DirectorsOfficers Enforcement
FedTracker FraudManipulation