

Statement

Stock Trading Plans Should Prevent – Not Enable – Insider Trading: Statement on Proposed Amendments to Rule 10b5-1



Commissioner Allison Herren Lee

Dec. 15, 2021

Working to keep markets fair by protecting against insider trading is one of the most fundamental jobs we have at the Commission. Enforcement in this area is key to our mission, but prophylactic measures designed to prevent the misconduct (rather than punish it after the fact) are vital. Because if companies and corporate insiders profit by trading on information that is available only to them, they not only disadvantage other shareholders, but also erode investor confidence and thereby undermine the integrity of our markets. So today's proposal seeks to ensure our rules are operating as intended to prevent, rather than shield, trading on inside information and bolster investor confidence in our markets.

* * *

Corporate insiders are routinely exposed to material nonpublic information. They also need to be able to trade fairly in the stock of their companies. Thus, the Commission adopted Rule 10b5-1 in 2000 to help clarify when liability may arise for insider trading.^[1] The rule sets forth certain conditions, which, if met, give rise to an affirmative defense against insider trading liability. Those conditions created a safe harbor for trading pursuant to a plan entered into in good faith before the person trading under the plan is aware of material nonpublic information.^[2] The idea being if a person establishes “a regular, pre-established program of buying or selling [their] company's securities,^[3]” that trading, when it later occurs, will not be considered to be on the basis of material nonpublic information potentially acquired after the adoption of the plan.

We've now had over two decades of experience with plans operating under this safe harbor. In that time, 10b5-1 plans have proliferated and lawmakers, regulators, courts, investors, and commentators have all observed the potential for abuse.^[4] Our ability to comprehensively evaluate the use of these plans is unfortunately hampered by the lack of related disclosure requirements. Nevertheless academic studies have produced compelling findings that suggest opportunistic use of 10b5-1 plans, including through such practices as trading shortly after the adoption of plans, and the use of multiple overlapping plans and single-trade plans.^[5] This is troubling evidence to suggest Rule 10b5-1 may be used to enable rather than avoid trading on the basis of inside information. Our rule should offer a safe harbor, not a pirates' cove.

So I am very pleased that today's proposal contains a package of amendments that would create new, common-sense conditions for the 10b5-1 safe harbor and enhance transparency around the use of 10b5-1 plans. In

particular, the proposal requires cooling-off periods for issuers and individuals after the adoption of plans before trading can commence, restricts the use of multiple overlapping plans and single-trade plans, and requires officers and directors to certify they are adopting plans in good faith and are not aware of material nonpublic information, among other measures.^[6] In addition, the proposal would impose new disclosure requirements, including quarterly disclosure regarding the adoption, termination, and terms of 10b5-1 plans, and disclosure of a company's insider trading policies and procedures.^[7] Taken together with the issuer share repurchase proposal we also consider today, the new disclosure requirements would considerably enhance transparency around issuer and executive trading in a company's securities and related policies, procedures, and practices.^[8]

The proposal seeks to curb potential abuses of our rules and enhance transparency for investors, while not unduly restricting issuer and individual trading in a company's securities for foreseeable, appropriate purposes. I hope the public will weigh in to help make sure we got the balance right. For example, are the cooling-off period durations—four months for individuals, 30 days for issuers—adequate? Is there sufficient need for single-trade plans to permit them under the safe harbor, or should they be prohibited altogether? Should the disclosure requirements be more specific regarding the policies and procedures information that investors may find useful? I look forward to reviewing comments on these and other aspects of the proposal.

* * *

I want to thank the staff for their thoughtful work on this proposal. With respect to this proposal and the other items we're considering today, I know you all have worked long and hard through the holiday season, and I'm very grateful for your dedication. I want to particularly commend Corey Klemmer in the Chair's Office for her hard work and thoughtful diplomacy in shepherding this proposal through the Commissioners' offices. Thank you and I'm pleased to support the proposal.

[1] See [Selective Disclosure and Insider Trading](#), Final Rule, Release No. 33-7881 (Aug. 15, 2000) ("This rule provides that a person trades 'on the basis of' material nonpublic information when the person purchases or sells securities while aware of the information.").

[2] *Id.* (explaining that the safe harbor "will be available only if the contract, instruction, or plan was entered into in good faith and not as part of a scheme to evade the prohibitions" of the rule").

[3] See [Selective Disclosure and Insider Trading](#), Proposed Rule, Release No. 33-7881 (Dec. 20, 1999) ("This provision is designed to apply in the case of an insider who wishes to establish a regular, pre-established program of buying or selling his or her company's securities.").

[4] See, e.g., [Waters and McHenry Introduce Bipartisan Legislation to Curb Illegal Insider Trading](#), Press Release (Jan. 18, 2019) (announcing the introduction of a bill, H.R. 624, the Promoting Transparent Standards for Corporate Insiders Act, to require the SEC to "consider certain types of amendments to Rule 10b5-1 that would ensure corporate insiders are unable to indirectly engage in illegal insider trading through changes to their trading plans"); [Letter from Chairman Jay Clayton to Congressman Brad Sherman](#) (Sept. 14, 2020) ("I believe that companies should strongly consider requiring all Rule 10b5-1 plans for senior executives and board members to include mandatory seasoning, or waiting periods after adoption, amendment or termination before trading under the plan may begin or recommence."); *In re Immucor Inc. Sec. Litig.*, 2006 WL 3000133, at *18 n.8 (N.D. Ga. Oct. 4, 2006) (noting that "a clever insider might maximize their gain from knowledge of an impending price drop over an extended amount of time, and seek to disguise their conduct with a 10b5-1 plan."); [Prepared Written Remarks of Jeffrey P. Mahoney General Counsel, Council of Institutional Investors, before U.S. Securities and Exchange Commission Investor Advisory Committee](#) (June 10, 2021) ("CII agrees that public confidence that our securities markets are fair to all participants serves the interests of companies and investors. And when public company executives conduct transactions in company stock through a 10b5-1 plan using practices that are inconsistent with the spirit of the rule, public confidence in corporate management teams and the markets can erode."); David F. Larcker, Bradford Lynch, Philip Quinn, Brian Tayan, and Daniel J. Taylor, [Gaming the System: Three "Red Flags" of](#)

[Potential 10b5-1 Abuse](#), Stanford Closer Look Series (Jan. 19, 2021) (“We show that a subset of executives use 10b5-1 plans to engage in opportunistic, large-scale selling of company shares.”).

[5] See Larcker et al., *supra* note 4 (identifying plans with short cooling-off periods, single-trade plans, and plans adopted in a given quarter that commence trading before the quarter’s earnings announcement as “red flags” of 10b5-1 abuses and finding that “[s]ales made pursuant to these plans avoid significant losses and foreshadow considerable stock price declines that are well in excess of industry peers”); see also Artur Hugon and Yen-Jung Lee, [SEC Rule 10b5-1 Plans and Strategic Trade around Earnings Announcements](#) (2016) (finding, among other things, “evidence consistent with insiders using 10b5-1 plans to sell stock in advance of disappointing earnings results”).

[6] As a condition of the availability of the affirmative defense under Rule 10b5-1, the proposal would impose a 120-day cooling-off period for officers and directors and a 30-day cooling off period for issuers, prohibit multiple overlapping plans for open market purchases or sales of the same class of securities, limit the use of single-trade plans to one per 12-month period, and require officer and director certifications. See Rule 10b5-1 and Insider Trading, Proposed Rule, Release No. 33-11013 (Dec. 15, 2021) [hereinafter *Proposing Release*].

[7] Specifically, the proposal would require quarterly disclosure of whether the issuer or any officer or director had adopted or terminated a plan during the last fiscal quarter, and information including the date of the adoption or termination, the duration of the plan, and the amount of securities to be purchased or sold under the plan. *Proposing Release* at 31-32. The proposal would also require issuers to disclose whether (and if not why not) a company has adopted insider trading policies and procedures, and if so, to disclose those policies and procedures. *Id.* at 35.

[8] Other features of the proposal include requiring that trading plans be operated in good faith as a condition of the safe harbor, requiring the structuring of disclosures under the rule, and requiring the reporting of dispositions of bona fide gifts of equity securities on Form 4.