

[Securities Regulation Daily Wrap Up, BENEFICIAL OWNERSHIP— S.D.N.Y.: An agreement increasing an exercise price was not a short-swing sale, \(Oct. 1, 2020\)](#)

Securities Regulation Daily Wrap Up

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By [Rodney F. Tonkovic, J.D.](#)

While the amount of profit was not known to the plaintiff, he was not required to specify a precise amount to adequately plead a claim under Section 16(b).

A district court allowed recovery of short-swing profits for one set of transactions in a shareholder suit bringing two claims. The court dismissed the first claim, finding that the complaint failed to plead a matching purchase and sale. The court denied the motion with respect for the second claim, however, finding that, at this stage, the complaint adequately pleaded the required purchase and sale by an insider within a six-month period, even though he did not specify the amount of profits realized by the defendants ([Rubenstein v. Knight-Swift Transportation Holdings Inc.](#), (September 30, 2020, Failla, K.).

The plaintiff owns shares of Knight-Swift, a publicly traded company listed on the New York Stock Exchange. Via various entities, the defendants beneficially own 40.8 million shares of Knight-Swift's common stock, representing 23.4% of the company's outstanding shares. During all the relevant times, the defendants beneficially owned over 10% of Knight-Swift's shares.

Transaction 1. The plaintiff first claimed that three transactions undertaken between December 2018 and February 2019 gave rise to liability under Section 16(b). In November 2017, one of the defendants' entities sold almost 5 million shares to an unrelated counterparty pursuant to a sale and repurchase agreement in exchange for a cash advance. In this case the repurchase agreement involved a sale in which the parties agree that the securities would be repurchased at any time at a pre-determined price.

The agreement was partially terminated on December 21, 2018 when the counterparty sold 1.5 million of the shares. The parties then amended the agreement as it pertained to the remaining shares to, among other items, increase the repurchase price. One week later the defendants' entity sold almost 1.2 million shares on the open market to Knight-Swift. Then, in February 2019, the repurchase agreement was terminated when the entity re-acquired all of its shares from the counterparty. These shares were then distributed to another of the defendants' entities to be sold to the counterparty under a variable pre-paid share forward (VPF) contract.

The court concluded that the plaintiff failed to state a claim with respect to these transactions. At issue was whether the partial termination of the repurchase agreement in December 2018 and its later amendment constituted a purchase that could be matched with the open market sale or the VPF transaction. The plaintiff maintained that the defendants' agreement constituted the acquisition of a new call equivalent position as to the outstanding shares.

The court explained that there is no case law or secondary source showing that an increase in the exercise price, as is the case here, and correspondingly a decrease in the call equivalent position, may be deemed a purchase. Plus, the court noted, "Rule 16b-6(a) is explicit that a decrease in a call equivalent position is a deemed sale." Since there were only sales, and no matching purchases, the court dismissed the first claim.

Transaction 2. The second claim involved a series of amendments in August 2019 to several outstanding VPF contracts, including the February 2019 VPF. The amendments increased the floor and cap prices, while the number of shares to be delivered remained unchanged. The VPF contracts were again amended in September 2019. Here, the defendants elected to amend the VPF with the February 2019 counterparty pursuant to a trigger

price agreement under which the defendants were also required to make a "commercially reasonable" payment to the counterparty in the amount of \$6,500,000.

The plaintiff alleged that each of the amended VPF transactions was a material amendment to previous contacts and was effectively a simultaneous disposition of each existing VPF and the establishment of a new VPF contract. That is, the disposition of the contacts was equivalent to the defendants purchasing the shares and the establishment of new VPFs was equivalent to a re-sale of the shares. The defendants did not dispute that the amendments equaled sales and repurchases, but argued instead that they did not realize any profit from these short-swing transactions.

The court found that the plaintiff stated a claim with respect to the September 2019 transactions. According to the court, the complaint explicitly claimed that there were profits from the transactions at issue—in an amount not known to the plaintiff—and seeks an accounting. Since the defendants cited no law showing that the plaintiff must provide an accounting of the profits at issue or that a Section 16(b) claim is subject to heightened pleading requirements, the motion to dismiss this claim was denied.

The case is [No. 1:19-cv-07802](#).

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Companies: Knight-Swift Transportation Holdings Inc.

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