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**10b5-1 TRADING PLANS:
PRACTICAL CONSIDERATIONS
FOR COMPANY INSIDERS**

by Michael Nordtvedt, Lisa Stimmell, Nicki Locker, Laurie Smilan, and Courtney Mathes

Directors, officers, and other company insiders often receive a meaningful portion of their overall compensation through equity awards. As these awards vest, many insiders seek to liquidate some or all of the underlying stock to access cash and diversify their investments. However, these insiders may find it difficult to liquidate their company stock because they are subject to certain legal and company-imposed restrictions that limit their ability to sell company stock.

- **Legal Restrictions.** Insider trading laws prohibit buying or selling stock whenever an insider is aware of material nonpublic information.
 - **Material.** Information is considered material if there is a substantial likelihood that a reasonable investor would consider it important in deciding whether to buy, sell, or hold company stock. While an analysis of whether company information is material or not is beyond the scope of this article, it is important to understand that materiality will be judged with the benefit of hindsight, particularly where the stock price reacts in response to subsequent disclosure of the previously-nonpublic information.
 - **Nonpublic.** Information is considered nonpublic if it is not widely available to investors and the public through the company's U.S. Securities and Exchange Commission (SEC) filings or media outlets.
- **Company-Imposed Restrictions.** Most companies have adopted insider trading policies in an effort to prevent insider trading by directors, officers, and employees, and to lessen their own legal risks. These policies tend to be more restrictive than insider trading laws and often include, among other things, trading blackout periods, which prohibit company

insiders from trading company stock prior to and immediately after the release of the company's quarterly earnings, without regard to whether company insiders are themselves aware of material nonpublic information.

In 2000, the SEC adopted Rule 10b5-1, which, among other things, provides an affirmative defense to insider trading claims for entities and individuals that have entered into binding trading plans for future purchases or sales of company shares.¹ If the entity or individual adopts a written trading plan in compliance with the requirements of Rule 10b5-1, then the Rule provides for this affirmative defense to claims by the SEC that trading was made on the basis of material nonpublic information, even if the entity or individual is in fact aware of material nonpublic information at the time of the trade.² An affirmative defense does not automatically eliminate liability; the company insider bears the burden of proving that:

- at a time when the company insider was not in possession of any material nonpublic information, the company insider entered into a 10b5-1 plan for trading securities;
- the 10b5-1 plan met all of the applicable requirements of Rule 10b5-1; and
- the purchase or sale of stock occurred in accordance with the terms of the 10b5-1 plan.

In addition, this affirmative defense is only available when the 10b5-1 plan was entered into in good faith and not as part of a plan or scheme to evade the prohibitions set forth in Rule 10b5-1. To realize the benefit of this affirmative defense, 10b5-1 plans must be constructed and designed carefully. The requirements set forth in Rule 10b5-1 provide that 10b5-1 plans must:

- specify the amount, price, and date of the transactions;
- specify an objective method for determining the amount, price, and date of the transactions; and
- place any subsequent discretion for determining the amount, price, and date of the transactions in another person who is not, at the time of any transaction, aware of material nonpublic information.

Company insider trading policies generally exempt trades made under 10b5-1 plans, subject in many cases to company approval of the 10b5-1 plan, from trading blackout periods and therefore, 10b5-1 plans go hand in hand with efforts to comply with restrictions imposed by law and those imposed by company policy. Drawing on experience over the past 20 years, we offer the following practical considerations for company insiders who are contemplating entering into a 10b5-1 plan for the sale³ of company stock.⁴

Entering into a 10b5-1 Plan

Assess whether a 10b5-1 plan is suitable for you.

Assess the potential benefits as well as the risks and limitations of adopting a 10b5-1 plan. These plans may not be appropriate for everyone.

The potential benefits of 10b5-1 plans may include:

- **Affirmative defense to insider trading actions by the SEC.** As discussed above, a compliant 10b5-1 plan affords an affirmative defense in insider trading actions by the SEC. Trades pursuant to 10b5-1 plans are also generally held by the courts to be not probative of intentional misconduct in shareholder securities class actions.

¹ See *Selective Disclosure and Insider Trading*, Release No. 33-7881 (Aug. 15, 2000) [65 FR 51715]. Rule 10b5-1 also includes a second affirmative defense solely for use by entities. This article focuses on 10b5-1 plan considerations for directors, officers, and other company insiders. Therefore, the second affirmative defense included in Rule 10b5-1 is beyond the scope of this article.

² In addition to written trading plans, the affirmative defense is also available for binding contracts to purchase or sell securities and for instructions made to another person to purchase or sell securities for the instructing person's account. This article focuses on written trading plans and these written trading plans are referenced throughout this article as 10b5-1 plans.

³ The focus of this article is on the sale of company stock by company insiders; however, it is important to note that 10b5-1 plans can also be used for the purchase of company stock.

⁴ These considerations do not constitute legal advice and are not a substitute for obtaining professional advice and assistance in connection with preparing and implementing a 10b5-1 plan.

- **Increased liquidity and financial diversification.** 10b5-1 plans can help facilitate financial planning for company insiders by providing greater certainty in planning trades, including providing for liquidity and diversification of stock portfolios, which may be particularly important in circumstances where a significant portion of compensation is paid in stock. In addition, 10b5-1 plans can also be used to meet specific financial planning objectives, for example,

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payment of a mortgage or college tuition.

- **More trading opportunities.** Trades under a 10b5-1 plan are oftentimes not subject to the blackout restrictions and pre-clearance requirements in company insider trading policies, allowing for more regular sales by company insiders.
- **Limiting adverse perceptions.** Sales of company stock by officers and directors are often scrutinized by investors and the media, particularly in light of the ready access to information relating to these sales.⁵ Sales pursuant to pre-authorized 10b5-1 plans are generally understood as less likely to be influenced by current material information or trends in the company's stock. Adverse perceptions of these sales

may be lessened if the company insider voluntarily discloses the existence of the 10b5-1 plan in the applicable Form 4 filings.

- **Administrative benefits.** Use of a 10b5-1 plan may enable company insiders to reduce the time spent executing trades (including obtaining any required pre-clearance of trades) and to manage their portfolio of company stock, including, for example, providing for the exercise of near-term expiring stock options.

The risks and limitations of 10b5-1 plans may include:

- **Reduced flexibility.** Use of a 10b5-1 plan requires planning and committing to trades and the trading schedule in advance, sometimes for as long as a year. In addition, for the reasons discussed below in the section entitled *Duration and Modification of 10b5-1 Plans*, once a 10b5-1 plan is in place, modifications and terminations of the 10b5-1 plan should be avoided and it is generally not recommended and, in many cases, impermissible under company policy, to sell company stock outside of the 10b5-1 plan. Therefore, 10b5-1 plans may not be desirable for those individuals who prefer to optimize their transactions based on movements in the stock price.
- **Affirmative defense must be proved.** As discussed above, the company insider has the burden of proving that the 10b5-1 plan satisfies the requirements set forth in Rule 10b5-1. Moreover, a 10b5-1 plan will not necessarily prevent someone from bringing a lawsuit and will not necessarily avoid adverse media coverage.
- **Time required to prepare a 10b5-1 plan.** The preparation of a 10b5-1 plan requires careful attention to ensure compliance with Rule 10b5-1 and all company-imposed requirements.
- **Criticism over potential abuse of 10b5-1 plans.** Investor groups, the media, the

federal government, and others have expressed concerns over the potential abuse of 10b5-1 plans by company insiders. Given these concerns, the SEC may give 10b5-1 plans a skeptical reading or decide to increase enforcement or investigative activity relating to 10b5-1 plans.

Allocate sufficient time to prepare a 10b5-1 plan.

The process of preparing a 10b5-1 plan and the related documentation, as well as working through the company's administrative requirements, may take some time, and you should plan accordingly. Companies generally require entry into 10b5-1 plans during open trading windows, that is, when there is no trading blackout period in effect. In addition, you must not have material nonpublic information when you enter into the 10b5-1 plan. Given these timing constraints, it is not advisable to start work on a 10b5-1 plan on the day prior to the company-imposed blackout period and expect that you will be able to complete the preparation and execution process in 24 hours.

Ensure that the 10b5-1 plan complies with all applicable law.

In preparing a 10b5-1 plan, your primary objective should be to ensure that all elements of 10b5-1 plan requirements are adequately addressed.

You should also be sure that the 10b5-1 plan complies with other applicable law. For example:

- **Rule 144.** Shares held by officers and directors are referred to as control securities and may only be sold in compliance with the applicable requirements of Rule 144 of the Securities Act of 1933. These requirements include, among others, ensuring that a Form 144 is filed prior to or concurrently with the sale (if the total amount of securities to be sold during any three-month period exceeds certain thresholds) and volume limitations on the number of shares of company

⁵ Directors and certain officers are required to file Form 4s with the SEC within two business days following a sale of company stock in the open market.

stock that the officer or director may sell during any three-month period. The 10b5-1 plan should provide for who will file the Form 144 and, if a broker will be executing the trades, that the broker will also facilitate compliance. In addition, officers and directors contemplating entry into a 10b5-1 plan should take into account Rule 144 volume limitations when devising trading instructions or formulas. While not generally advisable except in very narrow circumstances, if the company's insider trading policy permits trades outside of your 10b5-1 plan, or you are required to aggregate your sales with other parties who may be trading (for example, recipients of donations), then Rule 144 volume limitations may be particularly problematic. For example, based on SEC guidance, if the person entering into the 10b5-1 plan can control what portion of the volume limitation is available for 10b5-1 plan sales, then he or she is able to exercise influence over the 10b5-1 plan and the 10b5-1 defense would be unavailable.⁶ Because volume limitations will vary across companies and each individual's personal circumstances will differ, if you expect to engage in transactions outside of your 10b5-1 plan or are required to aggregate sales with other parties, it is generally advisable to discuss with your broker and counsel how best to manage compliance.

- **SEC filing requirements.** You should consider any burdens created by Rule 144 and Section 16 filing requirements when devising trading instructions or formulas. As noted above, officers and directors may be required to prepare and file one or more Form 144s with the SEC during the term of their 10b5-1 plans. Brokers generally can assist with these filings, but advance-planning is recommended. In addition, as noted, officers and directors are required to prepare and file Form 4s with the SEC for each sale of stock under their 10b5-1 plans. While multiple sales can be combined onto a single Form

4, these forms must be filed within two business days following each sale; therefore, frequent sales over the course of many days, weeks, or months, will require frequent Form 4 filings.

- **Short-swing liability.** In developing trading instructions or formulas, officers and directors should account for potential short-swing trading liability under Section 16(b) of the Securities Exchange Act of 1934, or the Exchange Act, if there will be both purchases and sales of company securities within any six-month period.

Ensure that the 10b5-1 plan complies with company-imposed requirements.

You should ensure that the 10b5-1 plan complies with any company-imposed requirements, which may be in addition to the requirements under Rule 10b5-1.

Company-imposed requirements may include, among other things, mandatory cooling-off periods after adoption or modification of the 10b5-1 plan and prior to the first transaction under the 10b5-1 plan, a minimum term for the 10b5-1 plan, limitations on modifications or termination of the 10b5-1 plan, limitations or prohibitions on trading in company securities outside of the 10b5-1 plan, and review or pre-clearance of the 10b5-1 plan by the company's compliance department.

These company-imposed requirements are generally adopted and enforced in order to ensure that 10b5-1 plans will be deemed adopted in good faith. While not included on the face of Rule 10b5-1, it is generally advisable for companies and for company insiders who adopt 10b5-1 plans, to adhere to guidelines such as a cooling-off period, limited modifications, limited or no terminations, and minimum terms, to ensure that the 10b5-1 plan provides protection from potential legal liability and reputational harm.

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Developing Trading Instructions

Given the flexibility of Rule 10b5-1 in relation to trading instructions, take time in developing your trading instructions.

Rule 10b5-1 allows significant flexibility in designing trading instructions or formulas. For example, you can:

- construct a matrix with different sale amounts at different price targets;
- base trading decisions on the performance of the company's stock against various market or industry indices, price gaps, or personal financial milestones;
- tie transactions to independent events, such as the timing of tuition or mortgage payments or other financial obligations;
- prioritize the sale (or exercise and sale) of particular securities based on factors such as tax treatment, tax basis, expiration dates, and exercise prices; and
- establish a 10b5-1 plan for a single transaction.

In addition to the flexibility accorded to trading instructions, various types of transactions may be structured to fit the requirements of Rule 10b5-1. For example, a 10b5-1 plan can cover pre-scheduled stock option exercises and sales. This may be helpful in avoiding a situation where a blackout period may effectively block exercise of an in-the-

⁶ See U.S. Securities and Exchange Commission, Division of Corporation Finance, Compliance and Disclosure Interpretations, Exchange Act Rules, Question 120.04 (Mar. 25, 2009).

money option that is about to expire because a same-day sale is necessary to fund payment of the exercise price and taxes. If properly structured, employee stock purchase plan transactions (including sales following a purchase) and 401(k) plan transactions can also qualify for the affirmative defense. While flexibility is permitted in preparing trading instructions under Rule 10b5-1, you will need to comply with any company-imposed requirements. In addition, there are other considerations to take into account with various approaches to trading instructions, some of which are discussed below.

Avoid unnecessarily complicated instructions.

You should be careful to avoid unnecessarily complicated instructions or formulas. Complicated instructions or formulas may result in mistakes in execution by the person administering the 10b5-1 plan (for example, due to a misunderstanding or misapplication of an instruction or formula or the failure to complete a calculation in time to exploit a market opportunity).

In general, instructions and formulas should be carefully and precisely drafted to avoid potential misunderstandings. You should try to provide as much detail as possible to facilitate the proper execution of the 10b5-1 plan. For example, if you possess several series of options, the 10b5-1 plan should specify which options to exercise. It may also be helpful to include examples of different scenarios in the instructions, and to review the trading instructions in advance with the person administering the 10b5-1 plan, to help ensure that you agree as to how the instructions or formulas are to operate.

Exercise caution when adopting 10b5-1 plans based on specific prices, floors, or ceilings.

Although Rule 10b5-1 permits 10b5-1 plans based on the market price on a particular date, a limit price, or a particular dollar price, if you are in a position to influence or control the timing of announcements of material news or events at the company, additional caution may

be warranted, at least in terms of the optics of future trading. In addition, these types of 10b5-1 plans may result in irregular trading patterns, which may be more susceptible to scrutiny. For further discussion, please see below under the heading *Consider whether expected trades under the 10b5-1 plan will coincide with significant future announcements or developments.*

If you intend to adopt a 10b5-1 plan with specific prices, floors, or ceilings,

Even though transactions executed in accordance with a properly designed 10b5-1 plan give rise to an affirmative defense against insider trading claims (and are oftentimes exempt from trading blackout periods under the company's insider trading policy), trades that occur at times shortly before a company announces material news may result in negative publicity for you and the company.

you should consider carefully the prices at which trades are to be executed. A 10b5-1 plan with specific prices, floors, or ceilings may result in periods of no stock sales, which may run counter to the reasons for adopting a 10b5-1 plan (that is, cash flow and portfolio diversification). Alternatively, price targets at a relatively low price may result in sales of too much stock at the lower price or result in questions from the market about insiders' faith in the future of the company. If your price targets are high relative to then existing prices, you may want to wait to establish a 10b5-1 plan until the targets are more achievable. By delaying the adoption of a 10b5-1 plan in that instance, you may be able to avoid risks associated with any subsequent modification or termination of an ineffective 10b5-1 plan.

Consider the expected magnitude and frequency of trades under the 10b5-1

plan generally and relative to the adoption of the 10b5-1 plan.

When preparing a 10b5-1 plan, you should give some consideration generally to the expected magnitude and frequency of trades under the 10b5-1 plan. There are pros and cons to smaller more frequent trades, and larger, event-based trades, so ultimately, your financial planning should be the controlling factor. However, the following are some aspects to consider:

- *Regular pattern of small sales.* A regular pattern of small sales may help to limit any inference that you sought to exploit material nonpublic information in developing your 10b5-1 plan; however, in the case of officers and directors, it will give rise to more frequent Form 4 filing obligations.
- *Occasional high-volume sales.* In contrast to a regular pattern of small sales, occasional high-volume sales may draw more attention and, if any of those sales turn out to precede bad news, may attract unwanted attention from the SEC, the media, investors, and private securities class action plaintiffs.

You may want to cap or otherwise limit the amount of potential sales for a particular period (for example, each week, month, quarter) to decrease the risk of unintended large sales, particularly if the 10b5-1 plan provides for cumulative sales if not all shares are sold in a given period or a certain dollar volume of sales is not achieved.

In addition, when preparing a 10b5-1 plan, you should give some consideration as to the expected magnitude and frequency of trades relative to the adoption of the 10b5-1 plan. Significant trading activity that occurs shortly after adoption of the 10b5-1 plan may raise suspicion as to whether the trades were based on material nonpublic information. It is generally advisable, and most companies enforce, a cooling-off period between adoption or modification of a 10b5-1 plan and the first trade thereunder to mitigate this concern.

Consider whether expected trades under the 10b5-1 plan will coincide with significant future announcements or developments.

When preparing a 10b5-1 plan, you should consider whether trades are expected to occur during quarterly trading blackout periods established under your company's insider trading policy (or around the time other significant announcements or developments involving the company are expected). Even though transactions executed in accordance with a properly designed 10b5-1 plan give rise to an affirmative defense against insider trading claims (and are oftentimes exempt from trading blackout periods under the company's insider trading policy), trades that occur at times shortly before a company announces material news may result in negative publicity for you and the company. In addition, trades that occur in the same general time frame as a significant announcement may raise questions as to whether the timing of the announcement was manipulated to your benefit. If you are generally indifferent as to the specific timing of a trade, consider avoiding trades during the expected time of your company's earnings announcements.

Duration and Modification of 10b5-1 Plans

Determine an appropriate duration for the 10b5-1 plan.

Although Rule 10b5-1 does not prescribe any limits on the duration of 10b5-1 plans, it is advisable to have 10b5-1 plans terminate after a certain period—we frequently see terms of approximately one year. This will force you to re-evaluate your trading instructions periodically and allows you to change your trading instructions (in conjunction with adopting a new 10b5-1 plan upon the scheduled expiration of the existing 10b5-1 plan) without raising any suspicions about the timing of those changes. It also allows you an opportunity to revert from a 10b5-1 plan to discretionary, non-plan trading without raising questions about the timing of that switch.

While it is important that you comply with any company-imposed requirements as to the minimum duration for 10b5-1 plans, you should also generally try to avoid adopting a 10b5-1 plan that has an unnecessarily long duration. The longer the duration, the greater the risk that circumstances may change such that

[M]odifications are generally treated as a new 10b5-1 plan, so they should always be made when you do not have material nonpublic information and in compliance with the requirements of Rule 10b5-1 and the company's policies regarding modifications.

you will have an incentive to modify or terminate the 10b5-1 plan. The modification or early termination of a 10b5-1 plan may create an implication that prior transactions under the 10b5-1 plan were not in fact pursuant to a *bona fide* 10b5-1 plan.

Avoid modifications and terminations to the extent possible, but account for the potential need to modify or terminate the 10b5-1 plan.

Rule 10b5-1 requires, among other things, that, to be covered by the affirmative defense, a transaction must occur pursuant to a 10b5-1 plan and the individual who entered into the 10b5-1 plan must not exercise influence after the fact. This requirement will not be satisfied if you alter or deviate from the 10b5-1 plan (whether by changing the amount, price, or timing of a purchase or sale) or if you enter into or alter a corresponding or hedging transaction or position with respect to transactions under the 10b5-1 plan. Depending on company-imposed requirements, some modifications may be permissible. However, modifications are generally treated as a new 10b5-1 plan, so they should always be made when you do not have material nonpublic information and in

compliance with the requirements of Rule 10b5-1 and the company's policies regarding modifications. In addition, while modifications to 10b5-1 plans are not explicitly restricted by Rule 10b5-1, if they are done frequently, then they may bring into question whether the 10b5-1 plan was entered in good faith and whether any prior transactions under the 10b5-1 plan were in fact made pursuant to a 10b5-1 plan for purposes of the requirements of Rule 10b5-1. Similarly, terminations may call into question whether a company insider entered into a 10b5-1 plan in good faith.

While modifications and terminations are discouraged, there may be situations in which market volatility or personal circumstances fundamentally alter the conditions under which you adopted the 10b5-1 plan. To anticipate this possibility, it is advisable that a 10b5-1 plan include formal provisions for its modification or termination, subject to any company-imposed requirements with respect to the modification of 10b5-1 plans. Such provisions will enable you to comply with the terms of the 10b5-1 plan while making the necessary changes. Altering the trades under the 10b5-1 plan or deviating from planned instructions without a formal modification is never advisable and, as noted above, will not be covered by the affirmative defense.

You should give careful consideration to those circumstances in which your 10b5-1 plan may be terminated without your consent. There are some standard termination provisions that brokers include in their form stock sale agreement for 10b5-1 plans that are generally acceptable and may not be negotiable, such as the announcement of the acquisition of the company or bankruptcy of the company, but if the 10b5-1 plan automatically terminates when you possess material nonpublic information, you may be prohibited from trading for an extended period until you are no longer in possession of material nonpublic information and out of a trading blackout. You may also want your 10b5-1 plan to provide for automatic termination upon certain changes in personal circumstances such as death, bankruptcy or insolvency, or divorce.

Even though the SEC has issued informal guidance that termination of a 10b5-1 plan on the basis of material nonpublic information does not, standing alone, violate Section 10(b) or Rule 10b-5 of the Exchange Act,⁷ any decision to terminate a 10b5-1 plan should be made judiciously and in consultation with your counsel.

Make accommodations for unexpected events that may warrant temporary suspension of trading under the 10b5-1 plan.

In preparing a 10b5-1 plan, you should make allowances for unforeseen events that may warrant automatic suspension of transactions under the 10b5-1 plan (for example, a proxy contest, tender offer, or merger). For example, Rule 14e-3 of the Exchange Act prohibits you from trading on material nonpublic information that relates to a tender offer of your company's stock. The affirmative defense under Rule 10b5-1 is not expressly applicable to potential liability under Rule 14e-3. Therefore, your 10b5-1 plan should require suspension or termination of the 10b5-1 plan when you become aware of a tender offer for your company's stock.

Using Brokers to Administer Your 10b5-1 Plan

Engage with an independent third-party administrator the 10b5-1 plan.

Generally, officers and directors will engage with a third-party stock brokerage firm or wealth manager to implement a 10b5-1 plan. Most well-known brokers and wealth managers have personnel who are experienced with 10b5-1 plans, have processes for implementing the 10b5-1 plan and associated trades, and have internal processes to aid in compliance issues. Some companies require use of a captive broker, meaning that company insiders are required to use a specific brokerage firm for their 10b5-1 plans. The captive broker will usually have a separate department that administers 10b5-1 plans and that implements appropriate ethical wall procedures.

Regardless of whether use of a captive broker is required, it is generally advisable to work with a broker that has a dedicated 10b5-1 plan department or personnel with experience following and executing complex instructions, as well as assisting directors and senior executives with compliance issues, including ensuring that the parameters of Rule 10b5-1 are followed and that Rule 144 and Section 16 filings are timely made. While 10b5-1 plans do not necessarily need to be administered by a third party and you do not, by the terms of Rule 10b5-1 need to use a broker, it is common practice and we believe best practice to do so. Accordingly, we refer primarily to "brokers" in the sections that follow, but other third parties may be engaged to administer your 10b5-1 plan and similar principles would apply.

Confirm that the broker has implemented procedures to ensure their independence.

Generally, brokers have a strong interest in ensuring that you and they comply with applicable law. To help ensure that the person administering your 10b5-1 plan is independent, your 10b5-1 plan could specify that:

- you and the person administering the 10b5-1 plan will only communicate in writing or via email (thereby documenting all communications in case of any future SEC inquiry),
- you will not communicate any information concerning the company or its securities to the person administering the 10b5-1 plan, and
- if you are using a broker, there are ethical wall procedures in place to restrict communications within the brokerage firm regarding the company and your trades.

To further address concerns as to the availability of the affirmative defense provided by a 10b5-1 plan, it may be helpful to include a provision in your agreement with the third party that pro-

vides for the suspension or termination of trading authority if the third party

Regardless of whether use of a captive broker is required, it is generally advisable to work with a broker that has a dedicated 10b5-1 plan department or personnel with experience following and executing complex instructions, as well as assisting directors and senior executives with compliance issues, including ensuring that the parameters of Rule 10b5-1 are followed and that Rule 144 and Section 16 filings are timely made.

becomes aware of material nonpublic information.

Protect your rights when working with brokers or other third parties.

When working with a broker or another third party in connection with a 10b5-1 plan, you will typically be expected to enter into some sort of agreement. Brokers will often have a standard form of stock sale agreement for purposes of implementing 10b5-1 plans. Your trading instructions would typically be included as a section of the stock sale agreement or attached to the stock sale agreement as an appendix or exhibit.

While brokers will often require that you use their form of agreement, most are generally amenable to some revisions to their standard forms.

It is strongly advised that you have an attorney review any proposed form of 10b5-1 plan for compliance with Rule 10b5-1 as well as to protect your legal rights generally and ensure you understand all of the terms of the 10b5-1 plan. You should expect that the broker

⁷ See U.S. Securities and Exchange Commission, Division of Corporation Finance, Compliance and Disclosure Interpretations, Exchange Act Rules, Questions 120.17 (Mar. 25, 2009) and 120.18 (Mar. 25, 2009).

or third party administering the 10b5-1 plan will request certain rights and protections (such as indemnification) that you should understand. Company counsel may review the 10b5-1 plan but remember that they represent the company's interests. Further, while you should consider recommendations and advice from the broker as to the 10b5-1 plan generally, you should set the trading instructions as you see fit.

Provide the broker with some flexibility in executing orders.

The 10b5-1 plan should provide some flexibility to the broker in executing orders in order to ensure that they occur as planned; as noted above, while the 10b5-1 plan may provide the broker with this flexibility, the company insider himself or herself may not retain any such discretion following adoption of the 10b5-1 plan. Factors such as insufficient trading volume and market volatility may prevent trades from being executed as planned, particularly if the 10b5-1 plan includes strict instructions with respect to the timing of transactions or provides for block purchases or sales. In addition, the use of a pre-designated date and time may lock you into a trade at an inopportune time (for example, when prices are unusually low). You should also consider how to handle any shortfalls that may occur if the person administering the 10b5-1 plan is unable or otherwise fails to effect all transactions specified in the 10b5-1 plan.

Consider delegating the precise timing of trades to the broker or other party administering the 10b5-1 plan.

Depending on the structure of your trading instructions, consider delegating discretion in the instructions in the 10b5-1 plan regarding the exact timing of trades, within a specified period (for example, five trading days), to the broker or other third party administering

the 10b5-1 plan. In order to maintain the affirmative defense, if discretion is provided to your broker, then your broker cannot be aware of any material nonpublic information. However, your broker may still be able to maximize proceeds from sales by taking into account publicly available information and general market trend information when determining the precise timing of trades depending on how you have structured the price targets, if any.

Hire legal and other advisors to assist in preparing the 10b5-1 plan.

You should hire your own advisors, including your own legal counsel, in connection with adopting a 10b5-1 plan and understanding the rules applicable to 10b5-1 plans. As a reminder, your company's legal counsel, both the in-house legal department, if any, and the outside legal counsel, represent the company, not you. Accordingly, neither the company nor its legal counsel are likely to assume responsibility for determining whether your 10b5-1 plan complies with Rule 10b5-1 regardless of any review or pre-clearance procedures.

Recent Developments

Since the adoption of Rule 10b5-1 in 2000, no further laws or regulations have been adopted to further define, expand, or limit the use of 10b5-1 plans or the associated affirmative defense. However, two bills, passed this year and last with overwhelming bipartisan support in the U.S. House of Representatives, proposed limits or restrictions on 10b5-1 plans.⁸

The first bill⁹ would require the SEC to consider amending Rule 10b5-1 to:

- 1) require that 10b5-1 plans are entered into only during open trading windows,

- 2) establish a mandatory cooling-off period after entering into a 10b5-1 plan and prior to the date of the first trade made under that plan,
- 3) limit the frequency of modifications or terminations of 10b5-1 plans,
- 4) require the filing of 10b5-1 plans, amendments, terminations, and transactions with the SEC, or
- 5) require that the board of directors of companies that have adopted 10b5-1 plans take certain actions relating to such 10b5-1 plans.

The second bill¹⁰ would require the SEC to issue rules that, in effect, would prohibit executive officers and directors from buying or selling company stock during the time period between the event requiring the filing of a Current Report on Form 8-K and the filing of the Form 8-K itself, referred to as the Form 8-K trading gap. The bill provides that the SEC could exempt transactions under a 10b5-1 plan so long as the 10b5-1 plan was not adopted during a Form 8-K trading gap.

Closing Thoughts

While not a panacea for scrutiny from transacting in your company's securities, 10b5-1 plans can be helpful in mitigating the risks associated with doing so. For those officers, directors, and company insiders considering a 10b5-1 plan, we offer the foregoing practical considerations as you navigate all of the requirements (both under Rule 10b5-1 and any company-imposed requirements) for 10b5-1 plans, as well as the choices generally available for formulating trading instructions.

⁸ As of the date of this article, both bills have been sent to the U.S. Senate Committee on Banking, Housing, and Urban Affairs but no further action has been scheduled.

⁹ On January 28, 2019, the U.S. House of Representatives passed H.R. 624, Promoting Transparent Standards for Corporate Insiders Act, by a vote of 413-3.

¹⁰ On January 13, 2020, the U.S. House of Representatives passed H.R. 4335, 8-K Trading Gap Act of 2019, by a vote of 384-7.

About the Authors:

Michael Nordtvedt is a partner and co-chair of the Capital Markets Practice at Wilson Sonsini, where he focuses on the representation of public and private technology, medical device, and life sciences companies through all stages of their growth, as well as investment banks and venture capital and private equity firms.

Lisa Stimmell is a partner and co-chair of the Public Company Representation Practice at Wilson Sonsini. Based in the firm's Palo Alto office, she practices corporate and securities law with a focus on advising public companies and larger enterprise clients on complex corporate governance, SEC compliance, and 1934 Act disclosure matters. She also advises late-stage private companies on enhancing governance structures and practices, as well as consideration of dual/multi-class governance structures. Lisa has a broad range of transactional experience, including the representation of public and private companies in mergers and acquisitions and other strategic transactions; underwriters and issuers in public offerings; and issuers and investors in private equity financings.

Nicki Locker is a partner and co-chair of the Securities Litigation Practice at Wilson Sonsini and has represented companies and their officers and directors in more than 200 shareholder class actions and derivative suits throughout the United States. She has also advised numerous boards and special committees in internal investigations regarding accounting improprieties, FCPA violations, stock option backdating, insider trading, off-label marketing, and embezzlement.

Laurie Smilan is Senior Of Counsel with the Securities Litigation Practice at Wilson Sonsini, where her practice focuses on securities litigation and counseling, and M&A and corporate governance matters. She has guided more than 100 public companies through securities and governance challenges, both in litigation and related investigations, and taught corporate governance at Georgetown University Law Center.

Courtney Mathes is a practice support lawyer in the Capital Markets and Public Company Representation Practices at Wilson Sonsini. Her legal experience includes practicing as an associate and counsel with the firm and several in-house legal counsel roles at public companies in the life sciences and technology sectors. She has primarily focused on corporate and securities law. In her current role, she leads or assists in the development and publication of substantive content projects, including client informational resources and thought leadership associated with capital markets and public companies.

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The firm also has more than 200 litigators, including securities and governance litigators in California, New York, Washington, D.C., Delaware, and Seattle. We represent public companies, private entities, and their officers and directors in securities and derivative actions in federal and state trial and appellate courts and SEC and regulatory proceedings as well as in connection with government and internal investigations and corporate governance matters. We have represented companies, their directors, and officers in other closely related types of litigation, including shareholder derivative lawsuits alleging breaches of fiduciary duties, and formal and informal investigations before the Securities and Exchange Commission and other regulatory agencies.

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650 Page Mill Road, Palo Alto, California 94304-1050 | Phone 650-493-9300 | Fax 650-493-6811 | www.wsgr.com

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