

## 10b5-1 Plans – Frequently Asked Questions

When planning to sell company stock, corporate executives and other “insiders” must navigate around “blackout periods” associated with the release of quarterly earnings, acquisitions, or other material events affecting the company. The blackout periods can significantly limit the windows of opportunity when insiders can buy and sell stock. Fortunately, 10b5-1 plans allow insiders to trade during blackout periods without violating insider-trading laws.

### What is a 10b5-1 plan?

Rule 10b5-1 permits insiders to adopt predetermined written plans for selling or purchasing specified amounts of stock as long as the person was not in possession of material, nonpublic information when the plan was adopted.

### What are the benefits of 10b5-1 plans?

These plans can be very valuable in helping insiders manage the wealth represented by company stock. The most important benefit of these plans is that a properly structured plan provides an affirmative defense against insider trading. Other benefits include:

- Access to secondary markets and liquidity during blackout periods
- Gradual diversification of concentrated equity positions at predictable intervals
- Alternative to bunching sales during open trading windows
- Mitigation of signaling issues associated with sales by insiders
- Convenience and predictability of putting the sale program on “auto pilot”
- Reduction of legal and compliance burden required to determine the materiality of nonpublic information for each trade

### What are the elements of 10b5-1 plans?

To serve as a valid affirmative defense against insider trading, a 10b5-1 plan must be adopted during an open trading window (i.e., outside a blackout period) and while the insider is not aware of material, nonpublic information. The plan must have been entered into in “good faith” and not as part of a plan to evade the prohibitions of Rule 10b5-1. The plan must also specify the amount, price, and timing of the transaction. As an alternative to specifying this information, the plan can use a written formula or algorithm to determine the price, amounts, and dates, or

the plan can provide instructions to another person to execute sales or purchases without the insider exercising any subsequent influence over how, when, or whether to effect the transaction.

### Why was Rule 10b5-1 created?

The Securities and Exchange Commission (SEC) enacted Rule 10b5-1 in October 2000 to provide added clarity around the prohibitions against insider trading. Before the rule went into effect, some courts interpreted insider trading as having occurred if the insider merely had “possession” of material, nonpublic information, while other courts interpreted insider trading as having occurred if the insider “used” the information in exercising the transaction.

Rule 10b5-1 creates more liability for insiders by adopting a broader “awareness” standard in relation to material, nonpublic information. The rule, however, provides greater ability for insiders to exercise trades by providing an affirmative defense against insider trading if the criteria discussed above are met.

### Can 10b5-1 plans be customized?

Rule 10b5-1 plans can be tailored to fit the insider’s overall wealth-management strategy and anticipated liquidity needs. The plan can be set up to sell a large block of shares at once or a certain number of shares each day, week, or month. A plan can also be created to sell shares once a certain price is hit. Alternatively, the timing and amount that is sold can be tied to anticipated events in the insider’s life, such as the expected months when children’s college tuition will be due.

### **Who can establish a 10b5-1 plan?**

Rule 10b5-1 plans can be established by any person who is not aware of material, nonpublic information at the time the plan is established. While these plans are most often used by corporate executives, board members, and other insiders, a person does not have to be an insider to establish a 10b5-1 plan.

### **Can a 10b5-1 plan be modified once it is established?**

Rule 10b5-1 plans can be modified once they have been established as long as the modification occurs at a time when the insider does not have access to material, nonpublic information. Modifying existing plans, however, can raise suspicions about why the insider is changing the plan. Any modifications to an existing plan should be made during an open trading window and preferably be tied to an external event in the insider's life, such as purchasing a new home.

### **Can trades be executed outside of the plan?**

An insider who has established a 10b5-1 plan may make trades of that security outside the plan, depending on the internal insider-trading policy of the issuer. The 10b5-1 affirmative defense will not apply to trades made outside the plan.

### **How do 10b5-1 plans relate to other SEC rules?**

A person trading through a 10b5-1 plan must still comply with all other SEC rules and other regulatory reporting requirements. If a person sells securities without registration under the Securities Act of 1933, the person may need to file a Form 144. The seller should indicate on the Form 144 that the sale is being made pursuant to a 10b5-1 plan.

### **Can a 10b5-1 plan conflict with the issuing company's trading policy?**

Any trades made through a Rule 10b5-1 plan are subject to the issuing company's trading restrictions, and some companies may not allow such trades. The company's insider-trading policy will typically indicate whether the company permits trades made through 10b5-1 plans. A company that allows these trades may require that additional guidelines be followed. Some companies may require approval of any 10b5-1 plan before the plan can be adopted. All companies, however, will require notice that a plan has been established.

### **Best practices in designing a 10b5-1 plan**

Based on our extensive experience working with corporate executives and board members to develop customized 10b5-1 plans, we recommend that plans consider incorporating the following guidelines:

- Establish the plan during an open trading window
- Consult with the company's legal and compliance officers when designing the plan
- Limit duration of the plan to one year or less; this allows for greater flexibility in adapting to changes related to market conditions and family circumstances
- Design the plan so that there are at least 30 days between when the plan is first adopted and when the first trade is executed through the plan
- Review the plan at least once a year to ensure that it still aligns with the insider's goals and circumstances
- Any modifications to an existing plan should be made during an open trading window and preferably be tied to an external event in the insider's life, such as purchasing a new home

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