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Client Alert

A report for clients and friends of the firm

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SEC Adopts Rules Restricting Insider Trading During Pension Fund Blackout Periods

As required by the Sarbanes-Oxley Act of 2002, the SEC (in Exchange Act Release No. 34-47225) on January 26, 2003 adopted rules prohibiting directors and executive officers of issuers, including foreign private issuers, from directly or indirectly purchasing, selling or otherwise acquiring or transferring any equity security of the issuer during a pension plan blackout period under which plan participants may not engage in transactions in securities held in their plan accounts. The prohibitions contained in this new Regulation Blackout Trading Restriction (BTR) under the Securities Exchange Act of 1934 apply only to securities acquired or disposed of by the director or executive officer if such securities were "acquired in connection with the executive officer's or director's service as a director or employment as an executive officer," which term is very broadly defined in the new rules. In addition, Regulation BTR provides that any equity securities transferred during a blackout period will be treated as though they had been acquired in connection with the director's or executive officer's service or employment, unless:

- the director or executive officer is able to establish that the securities were acquired from another source; and
- this identification is consistent with the treatment of the securities and tax purposes and other disclosure reporting requirements.

Acquisitions or dispositions of equity securities by family members, partnerships, trusts and other affiliates of a director or executive officer will be deemed to be acquisitions or dispositions by the director or executive officer if he or she had a pecuniary interest in the equity securities.

The trading prohibition is triggered only if the blackout period during which plan participants may not trade in securities in their individual plan accounts lasts for more than three consecutive business days; and

- in the case of a domestic issuer, this temporary suspension affects 50% or more of the participants under all pension plans with individual accounts maintained by the issuer; or
- in the case of a foreign private issuer, if the 50% test applicable to domestic issuers is satisfied and the number of U.S. plan participants subject to the temporary trading suspension is either (1) greater than 15% of the issuer's worldwide workforce or (2) greater than 50,000 in number.

Regulation BTR exempts from the statutory trading prohibition transactions that occur automatically, are made pursuant to an advance election or are otherwise outside the control of the director or executive officer, including:

- acquisitions of equity securities under dividend or interest reinvestment plans;
- purchases or sales of equity securities that satisfy the affirmative defense conditions of Exchange Act Rule 10b5-1(c);
- purchases or sales of equity securities, other than "discretionary transactions" (as defined in the Section 16 rules), under certain employee benefit plans;
- compensatory grants and awards of equity securities under programs where the grants and awards occur automatically;
- exercises, conversions or terminations of certain derivative securities, which, by their terms, occur only on a fixed date, or are exercised, converted or terminated by a counterparty who is not subject to the influence of the director or executive officer;
- acquisitions or dispositions of equity securities involving a bona fide gift or a transfer by will or the laws of descent and distribution;

- acquisitions or dispositions of equity securities under a domestic relations order;
- sales or dispositions compelled by law or other requirements of an applicable jurisdiction;
- sales or other dispositions of equity securities in connection with a merger, acquisition, divestiture or similar transaction occurring by operation of law; and
- increases or decreases in equity securities holdings resulting from a stock split, reverse stock split, stock dividend or pro rata rights distribution.

Regulation BTR requires that all issuers must provide timely notice (as specified in Rule 104(b)) to its directors and executive officers and, in the case of domestic issuers, file a notice with the SEC on Form 8-K of the imposition of a blackout period that triggers the trading prohibition. Foreign private issuers must file each such notice provided to its officers and directors during the preceding fiscal year as an exhibit to their annual report on Form 20-F, unless the notice was previously provided to the SEC on a Form 6-K.

Regulation BTR, including the notice requirement to directors and officers, is effective immediately, except that the obligation to give notice to the SEC on a Form 8-K of a blackout period is not effective until 60 days after the publication of Regulation BTR in the *Federal Register*, although issuers may provide such notice to the SEC under Item 5 ("Other Events and FD Disclosure") of Form 8-K or Item 5 ("Other Information") of Form 10-Q.

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Proskauer's Corporate Governance and Defense Practice consists of a multidisciplinary team of attorneys from our Corporate and Litigation practices, including renowned experts and former SEC and US Attorneys, who bring to bear considerable sophisticated expertise to serve your needs. Our Executive Compensation Practice also has capabilities in the area of Corporate Governance. The following individuals serve as the contact persons and would welcome any questions you might have.

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